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CITY OF SAN JOSE, CALIFORNIA

Single Audit Reports

Basic Financial Statements with
Federal Compliance Section

For the Year Ended June 30, 2008

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CITY OF SAN JOSE, CALIFORNIA

For the Year Ended June 30, 2008

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For the Year Ended June 30, 2008

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City Council
City of San José, California

Independent Auditor's Report

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of San José, California (the City), as of and for the year ended June 30, 2008, which collectively comprise the City's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the City's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the City's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of San José, California, as of June 30, 2008, and the respective changes in financial position and, where applicable, cash flows thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note I.E. to the financial statements, the City adopted the provisions of Governmental Accounting Standards Board (GASB) Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions* and GASB Statement No. 50, *Pension Disclosures—an amendment of GASB Statements No. 25 and No. 27.*

In accordance with *Government Auditing Standards*, we have also issued our report dated October 8, 2008, on our consideration of the City's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The management's discussion and analysis; the schedules of revenues, expenditures, and changes in fund balances – budget and actual for the General Fund and the Housing Activities Fund; and the schedules of funding progress listed in the table of contents are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and do not express an opinion on it.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City's basic financial statements. The accompanying schedule of expenditures of federal awards and schedule of revenues and expenditures of passenger facility charges are presented for purposes of additional analysis as required by OMB Circular A-133 and the *Passenger Facility Charges Guide,* respectively, and are not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, are fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Macias Gini & O'Connell LLP

Certified Public Accountants

Walnut Creek, California
October 8, 2008

Management's Discussion and Analysis

Management's Discussion and Analysis (MD&A) provides an overview of the City of San José's activities and financial performance for the fiscal year ended June 30, 2008. We encourage readers to read the MD&A in conjunction with the basic financial statements that immediately follow it, with the letter of transmittal at the beginning of the Introductory Section, and with other portions of this Comprehensive Annual Financial Report. All amounts have been rounded to the nearest one hundred thousand dollars and one tenth of a percent.

FINANCIAL HIGHLIGHTS

- Total assets exceed total liabilities at June 30, 2008 by $6.793 billion (net assets). Of this amount, unrestricted net assets of $377.4 million may be used to meet the City's ongoing obligations to citizens and creditors. In addition, restricted net assets of $823.0 million are dedicated to specific purposes and $5.592 billion is invested in capital assets, net of related debt.
- Total net assets decreased by $230.6 million or 3.3 percent during 2007-08 from $7.023 billion to $6.793 billion. Depreciation expense of $394.9 million accounts for this decrease. Excluding depreciation, net assets increased by $164.3 million.
- Governmental funds reported combined ending fund balances of $1.504 billion at June 30, 2008, which are $121.6 million or 8.8 percent more than the June 30, 2007 balances. Decreases in fund balances for the General Fund ($3.5 million), and other nonmajor funds ($30.7 million) were offset by the fund balance increases of the Redevelopment Agency ($85.2 million), Housing Activities ($69.4 million), Special Assessment Districts ($0.8 million) and San José Financing Authority Debt Service ($0.4 million). Unreserved fund balance comprises $759.8 million or 50.5 percent of combined governmental fund balances at June 30, 2008 and is available to meet the City's current and future spending needs at its discretion.
- Unreserved fund balance for the General Fund is $228.6 million at June 30, 2008 and represents 32.7 percent of total General Fund expenditures during 2007-08.
- Total long-term obligations increased by $810.5 million during 2007-08 to $5.129 billion at June 30, 2008, an increase of 18.8 percent over the amount at June 30, 2007. Primary factors leading to this increase during the year include the issuance of Redevelopment Agency tax allocation bonds and the issuance of Norman Y. Mineta San José International Airport revenue bonds.

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis provides an introduction to the City of San José's basic financial statements which are comprised of four components:

- Government-wide Financial Statements
- Fund Financial Statements
- Notes to the Basic Financial Statements
- Required Supplementary Information

In addition, this report also contains other supplementary information.

Government-wide Financial Statements

Government-wide Financial Statements provide readers with a broad overview of the City of San José's finances in a manner similar to that of a private-sector business.

The ***statement of net assets*** presents information on all assets and liabilities and reports the difference between the two as *net assets.* Over time, increases or decreases in net assets may serve as a useful indicator of whether the City's financial position is improving or deteriorating.

The ***statement of activities*** presents information showing how the net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will result in cash flows in future fiscal periods. Examples include revenues pertaining to uncollected taxes and expenses pertaining to earned but unused vacation and sick leave.

Both of these government-wide financial statements address functions that principally are supported by taxes and intergovernmental revenues (*governmental activities)* and other functions that intend to recover all or in part a portion of their costs through user fees and charges (*business-type activities).* The governmental activities of the City of San José include general government, public safety, capital maintenance, community services, and sanitation. Its business-type activities include airport, wastewater treatment, water supply, and various parking management operations.

The government-wide financial statements include not only the primary government of the City of San José, but also a legally separate redevelopment agency and three legally separate financing authorities for which the City is financially accountable.

Fund Financial Statements

Fund Financial Statements report information about groupings of related accounts used to maintain control over resources segregated for specific activities or objectives. As do other state and local governments, the City of San José uses fund accounting to ensure and demonstrate finance-related legal compliance. Each City fund falls into one of three categories: *governmental funds, proprietary funds,* or *fiduciary funds*.

Governmental funds account for essentially the same functions reported as *governmental activities* in the government-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on *near-term inflows* and *outflows of spendable resources,* as well as on *balances of spendable resources* available at the end of the fiscal year. Such information may be useful in evaluating the City of San José's capacity to finance its programs in the near future.

Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for *governmental funds* with similar information presented for *governmental activities* in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near-term financing decisions. Both the governmental funds balance sheet and the governmental funds statement of revenues, expenditures and changes in fund balances provide a reconciliation to facilitate comparison between *governmental funds* and *governmental activities.*

The governmental funds balance sheet and the governmental funds statement of revenues, expenditures and changes in fund balances present information separately for the General Fund, Redevelopment Agency, Housing Activities, Special Assessment Districts, and the San José Financing Authority Debt Service, which are all classified as major funds. These statements also report several individual governmental funds classified as nonmajor funds such as special revenue, debt service, and capital projects funds which are combined into a single, aggregated presentation. Individual fund data for each of the nonmajor governmental funds is provided in the form of *combining statements* elsewhere in this report.

The City of San José adopts an annual appropriated budget for its General Fund and Housing Activities. This report includes budgetary comparison statements to demonstrate compliance with these budgets.

Proprietary funds generally account for services charged to external or internal customers through fees. Proprietary funds provide the same type of information as shown in the government-wide financial statements for *business-type activities*, only in more detail. The City of San José accounts for its airport, wastewater treatment, water supply, and parking management operations in proprietary funds.

Fiduciary funds account for resources held for the benefit of City of San José employees and outside parties in a similar manner as that for proprietary funds. Pension plan trust funds, private purpose trust funds, and agency funds are reported as fiduciary funds. The government-wide financial statements do not include fiduciary funds as their resources are not available to support City of San José programs.

Notes to the Basic Financial Statements provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements.

Required Supplementary Information includes the budgetary schedules for General Fund and Housing Activities. In addition, pension schedules present the City of San José's progress towards funding its obligation to provide future pension benefits for its active and retired employees.

Combining and individual fund statements and schedules referred to earlier provide information for nonmajor governmental funds and fiduciary funds and are presented immediately following the required supplementary information.

GOVERNMENT-WIDE FINANCIAL ANALYSIS

Analysis of net assets: As noted earlier, net assets may serve as a useful indicator of a government's financial position. For the City of San José, assets exceeded liabilities by $6.793 billion at the June 30, 2008 close of the current fiscal year.

The following table is a condensed summary of the City's net assets for governmental and business-type activities:

Statement of Net Assets
June 30, 2008 and 2007
(in thousands)

	Governmental Activities		Business-type Activities		Totals	
	FY 2008	FY 2007	FY 2008	FY 2007	FY 2008	FY 2007
Assets:						
Current and other assets........ $	1,951,906	1,839,606	1,112,121	597,993	3,064,027	2,437,599
Capital assets.....................	7,806,763	7,952,920	1,621,811	1,374,028	9,428,574	9,326,948
Total assets................	9,758,669	9,792,526	2,733,932	1,972,021	12,492,601	11,764,547
Liabilities:						
Current and other liabilities.....	301,689	321,904	268,948	100,591	570,637	422,495
Long-term liabilities...............	3,929,063	3,696,129	1,200,114	622,542	5,129,177	4,318,671
Total liabilities............	4,230,752	4,018,033	1,469,062	723,133	5,699,814	4,741,166
Net assets:						
Invested in capital assets, net of related debt............	4,769,191	5,193,578	823,223	750,334	5,592,414	5,943,912
Restricted net assets............	662,863	501,391	160,153	248,039	823,016	749,430
Unrestricted net assets..........	95,863	79,524	281,494	250,515	377,357	330,039
Total net assets........... $	5,527,917	5,774,493	1,264,870	1,248,888	6,792,787	7,023,381

At June 30, 2008, the City of San José reported positive balances in all three categories of net assets, both for the City as a whole, as well as for its separate governmental and business-type activities.

At $5.592 billion, investment in capital assets (infrastructure, land, buildings, other improvements, vehicles, and equipment, less outstanding debt used to acquire them) comprise 82.3 percent of the City of San José's total net assets. Since these assets are not liquid and they provide services to citizens, they are not available for future spending.

Of the total net assets, $377.4 million or 5.6 percent represents unrestricted net assets available for meeting the City's ongoing obligations to citizens and creditors. Governmental activities show a positive balance of $95.9 million in unrestricted net assets and business-type activities show a positive balance of $281.5 million. An additional portion of the City's net assets representing $823.0 million or 12.1 percent of the total are subject to legal restrictions on their use.

During 2007-08, the City of San José's net assets decreased by $230.6 million or 3.3 percent. Nonetheless, revenues increased at a faster rate than expenses during the year which narrowed the revenue shortfall for 2007-08. This is a slight improvement over 2006-07 when expenses outpaced revenues by $233.5 million.

Notable changes in the statement of net assets between June 30, 2008 and June 30, 2007 include:

- Capital assets increased by $101.6 million or 1.1 percent compared to the prior fiscal year. Governmental capital assets decreased by $146.2 million, but were offset by an increase in business-type capital assets of $247.8 million. The decrease in governmental capital assets resulted from asset additions of $203.4 million less $345.6 million in depreciation expense for major infrastructure and other assets and asset deletions of $4.0 million. The increase in business-type capital assets was due primarily to continued airport expansion construction projects in the amount of $273.2 million which was partially offset by business-type activities depreciation expense of $49.3 million.

- Current and other assets increased by $626.4 million or 25.7 percent due to a $112.3 million increase for governmental activities and a $514.1 million increase for business-type activities. The increase for governmental activities primarily resulted from unspent Redevelopment Agency bond proceeds and a decrease in allowance for doubtful accounts for receivables from developers of various housing projects. The increase for business-type activities was due to unspent bond proceeds for the Norman Y. Mineta San José International Airport (Airport).

- Long-term liabilities increased by a net amount of $810.5 million or 18.8 percent principally due to the issuance of Redevelopment Agency tax allocation bonds, Series 2007A-T and Series 2007B, and Airport revenue bonds, Series 2007A and Series 2007B. The increase was partially offset by the refunding of Airport revenue bonds, Series 2004A and Series 2004B, which were refunded through the issuance of short term commercial paper notes.

- Current and other liabilities for the City increased by $148.1 million or 35.1 percent, primarily due to a $144.8 million increase in short term notes payable related to the Airport commercial paper program. The proceeds of the Airport commercial paper notes were used to refund the City's outstanding Airport revenue bonds, Series 2004A and Series 2004B.

- Net assets invested in capital assets, net of related debt decreased $351.5 million or 5.9 percent. While the business-type activities increased by $72.9 million, general government activities accounted for the overall result with a decrease of $424.4 million. The $424.4 million decrease is due mainly to depreciation expense of $345.6 million exceeding net current year additions to capital assets of $199.5 million and an increase in debt principally related to the issuance of Redevelopment Agency tax allocation bonds.

Analysis of activities: The following table indicates the changes in net assets for governmental and business-type activities:

Statement of Activities
For the Year Ended June 30, 2008 and 2007
(in thousands)

	Governmental Activities		Business-type Activities		Totals	
	FY 2008	FY 2007	FY 2008	FY 2007	FY 2008	FY 2007
Revenues:						
Program revenues:						
Fees, fines, and charges for services.......... $	325,853	273,679	303,480	264,926	629,333	538,605
Operating grants and contributions..............	94,357	93,090	8,444	8,284	102,801	101,374
Capital grants and contributions..................	48,075	68,835	9,162	17,927	57,237	86,762
General revenues:						
Property taxes...	495,731	467,917	-	-	495,731	467,917
Utility taxes...	82,255	79,129	-	-	82,255	79,129
Franchise taxes..	41,064	40,415	-	-	41,064	40,415
Transient occupancy taxes.........................	23,900	21,400	-	-	23,900	21,400
Sales taxes shared revenue........................	149,500	145,340	-	-	149,500	145,340
State of California in-lieu............................	9,244	5,911	-	-	9,244	5,911
Business license tax.................................	39,901	39,502	-	-	39,901	39,502
Unrestricted interest and investment earnings.	65,721	39,359	29,232	21,138	94,953	60,497
Other revenue...	53,420	35,875	-	-	53,420	35,875
Total revenues......................................	1,429,021	1,310,452	350,318	312,275	1,779,339	1,622,727
Expenses:						
General government................................	142,886	120,362	-	-	142,886	120,362
Public safety...	476,570	393,449	-	-	476,570	393,449
Capital maintenance.................................	569,636	528,727	-	-	569,636	528,727
Community services.................................	211,511	276,343	-	-	211,511	276,343
Sanitation...	113,525	99,720	-	-	113,525	99,720
Interest and fiscal charges.........................	170,852	154,135	-	-	170,852	154,135
Norman Y. Mineta San José International Airport..	-	-	153,927	139,623	153,927	139,623
Wastewater Treatment System....................	-	-	134,882	111,435	134,882	111,435
Municipal Water System............................	-	-	26,017	22,618	26,017	22,618
Parking System.......................................	-	-	10,127	9,787	10,127	9,787
Total expenses.....................................	1,684,980	1,572,736	324,953	283,463	2,009,933	1,856,199
Excess (deficiency) before transfers	(255,959)	(262,284)	25,365	28,812	(230,594)	(233,472)
Transfers..	9,383	6,418	(9,383)	(6,418)	-	-
Change in net assets............................	(246,576)	(255,866)	15,982	22,394	(230,594)	(233,472)
Net assets at beginning of year	5,774,493	6,030,359	1,248,888	1,226,494	7,023,381	7,256,853
Net assets at end of year........................... $	5,527,917	5,774,493	1,264,870	1,248,888	6,792,787	7,023,381

Governmental activities: Net assets for governmental activities decreased by $246.6 million or 4.3 percent during 2007-08 from $5.774 billion to $5.528 billion. Total revenues increased at a rate of 9.1 percent compared to expenses increasing at a rate of 7.1 percent. During 2006-07, revenues and expenses increased at rates of 8.5 percent and 4.7 percent, respectively.

Significant elements of the decrease in net assets for governmental activities from June 30, 2007 to June 30, 2008 are as follows:

- General government expenses increased by $22.5 million or 18.7 percent between years primarily due to the recognition of the City's underfunding of the current year other postemployment benefits annual required contribution and the net loss incurred on the disposal of assets.

- Public safety expenses increased by $83.1 million or 21.1 percent higher than the previous year primarily due to negotiated higher wage, pension, healthcare and benefit costs, and the recognition of the City's underfunding of the current year other postemployment benefits annual required contribution.

- Capital maintenance expenses increased by $40.9 million or 7.7 percent between years primarily due to increases in street resurfacing and Redevelopment Agency project related expenditures.

- Community services expenses decreased by $64.8 million or 23.5 percent due mainly to an increase in allowance for doubtful accounts for receivables from developers of various housing projects in the previous year being followed by a decrease in the current year.

- Sanitation expenses increased by $13.8 million or 13.8 percent between years due to integrated waste management rate increases.

- Depreciation expense for infrastructure and other capital assets was $345.6 million, an increase of 1.7 percent.

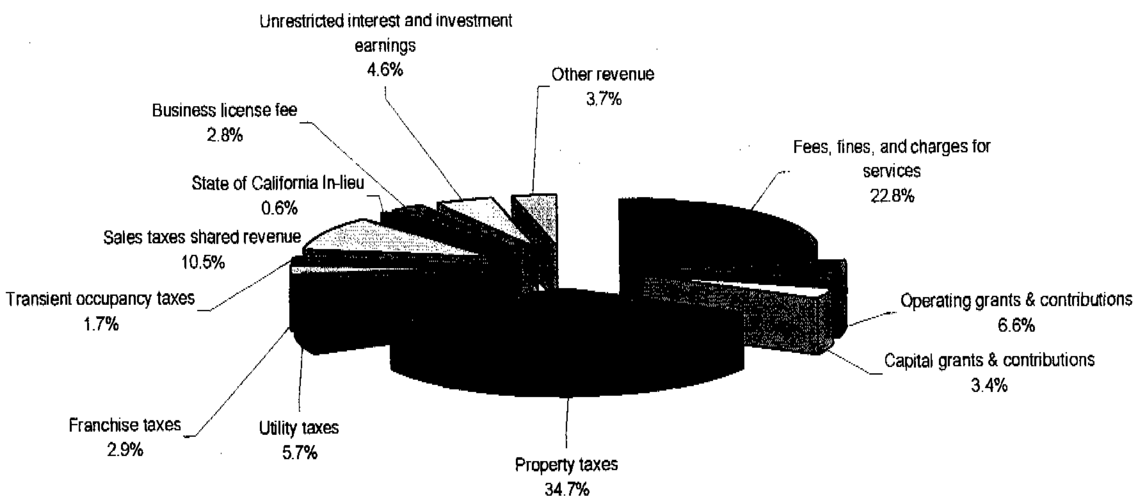
- Contributing to the increase in total revenues, property tax revenue increased by $27.8 million or 5.9 percent primarily due to modest growth in secured property tax revenue related to both the residential and commercial sectors. Fees, fines and charges for services also increased by $52.2 million or 19.1 percent due primarily to rate increases for integrated waste management services, as well as increases in storm drainage service use charges, convention and cultural facilities rental revenue, and the establishment of a North San José traffic impact fee.

- Capital and operating grants and contributions decreased by $19.5 million or 12.0 percent principally due to reduced federal funding for Workforce Investment Act (WIA) grants and Urban Areas Security Initiative (UASI) grants.

- In addition, utility taxes, franchise taxes, transient occupancy taxes, sales taxes, State of California in-lieu revenue, business license tax, and other revenue experienced an aggregate increase of $31.7 million or 8.6 percent. Some factors contributing to the overall increase include net increases in average hotel room rates and occupancy rates, and utility rates.

- Annualized investment interest yield decreased from 4.7 percent as of June 30, 2007 to 4.1 percent as of June 30, 2008. The earned interest yield reflects the lower interest rate environment experienced during the year; however, the total portfolio value as of June 30, 2008 increased by $83.7 million over June 30, 2007, contributing to an overall increase in interest and investment earnings of $26.4 million or 67.0 percent.

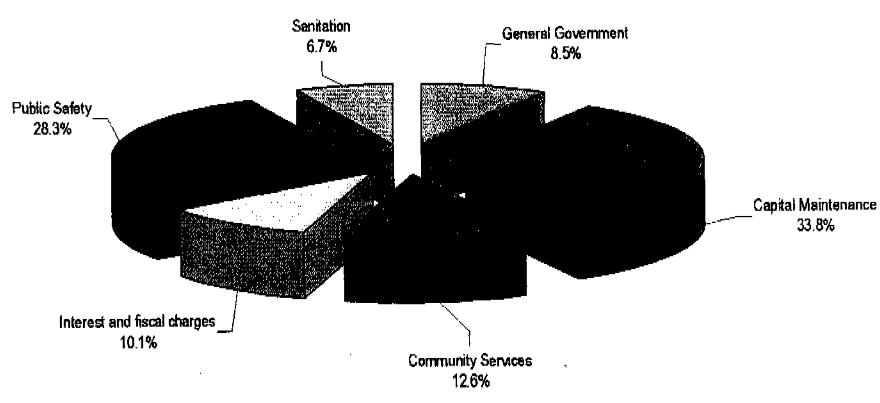
Revenue 2008



The chart above shows the principal components of 2007-08 revenue sources for governmental activities. Of the $1.429 billion in total revenues generated by governmental activities, 68.0 percent is attributable to property taxes (34.7 percent), fees, fines, and charges for services (22.8 percent), and sales taxes (10.5 percent). The overall percentage of revenues for these categories is consistent with 2006-07.

The chart below shows the principal categories of 2007-08 expenses for governmental activities. Of the $1.685 billion in total expenses generated by governmental activities, the categories accounting for 74.6 percent of the total are capital maintenance (33.8 percent), public safety (28.3 percent), and community services (12.6 percent). The overall percentage of expenses for public safety increased by 3.3 percent over 2006-07 due to higher wage, pension, healthcare and benefit costs, and the recognition of the City's underfunding of the current year other postemployment benefits annual required contribution. The overall percentage of expenses for community services decreased by 5.0 percent primarily due to a decrease in allowance for doubtful accounts for receivables from developers of various housing projects.

Expenses 2008



Business-type activities: Business-type activities net assets increased by $16.0 million or 1.3 percent to $1.265 billion during 2007-08.

The notable components of the increase in net assets for business-type activities during 2007-08 are:

- The Norman Y. Mineta San José International Airport (Airport) net assets increased by $14.2 million or 3.4 percent. The Airport incurred an operating loss of $27.3 million in 2007-08, a decrease of $5.1 million or 15.8 percent compared to the 2006-07 loss of $32.4 million. Operating revenues increased by $19.7 million or 20.7 percent reflecting higher rental and concessions revenue. Operating expenses of $142.2 million in 2007-08 were 11.4 percent higher compared to 2006-07, highlighted by an $9.6 million increase in operating and maintenance costs. Nonoperating revenues exceeded nonoperating expenses in 2007-08 by $35.8 million, an increase of $6.8 million or 23.4 percent from 2006-07. An increase in investment income of $6.5 million accounted for the majority of the increase due to larger cash balances resulting from the issuance of Airport revenue bonds Series 2007A and Series 2007B. In addition, the Airport received $5.0 million in capital contributions primarily from Airport Improvement Program grants.

- Wastewater Treatment System net assets increased by $3.5 million or less than 1.0 percent from $658.6 million to $662.1 million. Operating revenues increased $11.4 million or 10.0 percent from $113.7 million in 2006-07 to $125.1 million in 2007-08 primarily due to a sewer service rate increase of 9.0 percent. Total operating expenses increased by $23.8 million or 22.2 percent primarily due to higher operations and maintenance and depreciation and amortization costs associated with newly completed capital projects. Nonoperating revenues increased by $6.0 million attributable primarily to an increase in other revenues of $4.4 million due mainly to easement settlements with utility companies. Transfers-out of $7.5 million in 2007-08 consisting primarily of transfers to the General Fund for in-lieu taxes and the City's portion of a utility company settlement represent an increase of $2.2 million compared to 2006-07.

- Municipal Water System net assets decreased by $2.3 million or 2.7 percent from $84.7 million to $82.4 million. Operating revenues of $24.0 million increased $1.6 million or 7.4 percent from $22.4 million due mainly to rate increases. Offsetting this gain, operating expenses of $25.8 million increased $3.4 million or 15.3 percent from $22.4 million primarily due to higher operations and maintenance costs for upgrades to facilities to meet customer needs and comply with regulatory requirements. Capital contributions of $0.2 million decreased $3.7 million or 95.2 percent from $3.9 million resulting from a decrease in donated assets from developers.

- Parking System net assets increased by $0.6 million or less than 1.0 percent from $91.1 million to $91.7 million. Operating revenues increased $1.4 million or 13.8 percent due primarily to increased rates. Operating expenses also increased by $0.3 million or 3.5 percent reflecting mainly higher depreciation and amortization costs.

FINANCIAL ANALYSIS OF THE CITY'S FUNDS

As noted earlier, the City uses ***fund accounting*** to ensure and demonstrate compliance with finance-related legal requirements.

Governmental funds

The City of San José's governmental funds provide information about near-term inflows, outflows, and resources balances available for spending. Such information is useful in assessing the City's financial requirements for its programs and activities. In particular, unreserved fund balance at the fiscal year end may serve as a useful measure of a government's capacity for spending in future years. Governmental funds reported by the City of San José include the General Fund, Special Revenue Funds, Debt Service Funds, and Capital Project Funds.

As of June 30, 2008, the City's governmental funds reported combined fund balances of $1.504 billion, an increase of $121.6 million or 8.8 percent compared to the balance at June 30, 2007. *Unreserved fund* *balance* at $759.8 million constitutes 50.5 percent of the combined balances and is available for spending at the City's discretion. The $743.9 million remainder of the governmental fund balances is *reserved* to indicate that it is *not* available for new spending because the following portions have been committed to particular purposes:

- $301.3 million for advances, loans, and other assets that are long-term in nature and thus do not represent currently available resources;
- $288.8 million for contractual commitments of 2007-08 carried into fiscal year 2008-09;
- $153.4 million for debt service payable in fiscal year 2008-09;
- $0.4 million for restricted cash commitments.

Revenues and other financing sources for governmental functions totaled approximately $2.106 billion in 2007-08, a decrease of $449.1 million or 17.6 percent from 2006-07 primarily due to the use of a one-time funding source in the prior year (redevelopment agency refunding bonds of $701.2 million).

General Fund: The General Fund is the chief operating fund of the City of San José. At June 30, 2008, its unreserved fund balance is $228.6 million or 82.5 percent of the $277.1 million total General Fund balance. Comparing both unreserved fund balance and total fund balance to total fund expenditures may be useful as a measure of the General Fund's capacity to liquidate future obligations. At June 30, 2008, unreserved fund balance represents 32.7 percent of total General Fund expenditures of $699.1 million, while total fund balance represents 39.6 percent. This measure of financial health shows a modest decline from the prior fiscal year. At June 30, 2007, the same measures were 38.7 percent and 44.3 percent respectively of $633.0 million in 2006-07 expenditures.

As anticipated at the beginning of the year, slight growth in key revenue sources in 2007-08 was not sufficient to meet all expenditure obligations. However, the use of reserves and one-time revenues offset by net transfers into the General Fund resulted in a $3.5 million or 1.2 percent decrease to the General Fund balance during 2007-08.

In 2007-08, General Fund revenues of $694.4 million were $20.1 million or 3.0 percent higher than 2006-07 revenues of $674.3 million. Due to a slowing economy, this increase reflects the smallest growth rate in General Fund revenues since fiscal year 2003-04. The current year increase is due primarily to increases in property tax revenue of $11.9 million and sales tax revenue of $4.0 million, offset slightly by a decrease in intergovernmental revenue of $7.7 million due to a reduction in revenue received from the federal government related to the Urban Areas Security Initiative (UASI) and Super UASI grants.

General Fund expenditures of $699.1 million in 2007-08 were $66.1 million or 10.4 percent higher than 2006-07 expenditures of $633.0 million. The increase in expenditures was mainly due to increases in public safety of $47.4 million because of higher wage, pension, healthcare and benefit costs and community services of $12.8 million related to providing services and maintenance requirements to new City facilities.

Redevelopment funds: The Redevelopment Agency (Agency) fund accounts for the activities of the Redevelopment Agency of the City of San José that redevelops and upgrades blighted areas. Fund balance for the Agency's governmental funds increased $85.2 million or 69.8 percent to $207.2 million at June 30, 2008. A deficit of expenditures over revenues of $87.0 million was offset by other financing sources (net) of $172.2 million.

The following are some of the highlights for the Agency:

- Revenues increased by $34.0 million or 19.3 percent to $210.2 million from $176.2 million in the prior fiscal year. This increase is primarily due to a $23.1 million increase in tax increment revenue, attributable mainly to increased commercial and industrial property values.

- Expenditures increased $31.0 million, or 11.7 percent from the prior fiscal year. This increase was attributable primarily to capital outlay expenditures for building public facilities and payment to the County of Santa Clara (County) for a share of proceeds of redevelopment bond issues as defined in a 2001 agreement between the Agency and the County.

- Other financing sources increased $87.8 million over other financing sources of $84.4 million in 2006-07. The primary source of this increase was the issuance of Tax Allocation Taxable Bonds Series 2007A-T for $12.9 million and Tax Allocation Tax Exempt Bonds Series 2007 B for $200.0 million.

Additional information about the Agency's finances appears in their separately issued financial statements.

Housing funds: The Housing Activities fund accounts for the City of San José's commitment to providing low and moderate income residents with a diverse range of safe, decent, and affordable housing opportunities. Objectives include preserving the existing affordable housing stock, increasing the supply of affordable housing, and providing services to homeless and at-risk populations. Redevelopment Agency tax allocation bonds and 20 percent of the gross property tax increment provide the fund's primary resources. As required by California State law, the tax increment revenue is used solely for affordable housing. The fund's loans receivable balance (net) which represents loans to developers of various affordable housing projects increased during the current year by $63.9 million or 31.3 percent to $268.3 million at June 30, 2008 due to an increase in loans to developers for various projects including the Almaden Family, Hillsdale Townhouse and King Crossing housing projects, and a decrease in the valuation allowance in the Housing Activities Fund based on the City's review of the valuation accounts.

Total expenditures decreased by $75.6 million or 97.8 percent to $1.7 million from $77.3 million in the prior fiscal year, which is primarily due to a decrease in allowance for doubtful accounts for receivables from developers of various housing projects.

Special assessment funds: The Special Assessment Districts fund accounts for debt issuance and capital improvements related to the specific purposes of eight special assessment and community facilities districts located in different parts of the City of San José. A total of $68.2 million in special assessment debt outstanding at June 30, 2008 is secured by special assessments or taxes charged to owners' real property in the district issuing the debt. The City of San José is not obligated to cure any deficiency or redeem any debt of special assessment districts. However, the City may voluntarily choose to cure a deficiency at its sole discretion. There was no new special assessment debt issued during 2007-08.

Total expenditures decreased by $16.1 million or 66.8 percent to $8.0 million from $24.1 million in the prior fiscal year. This decrease is primarily due to a one-time prior year $11.1 million reimbursement of development costs to the developers of the Evergreen Specific Plan Property Ownership Partnership.

Financing authority funds: The San José Financing Authority Debt Service fund accounts for the issuance of commercial paper notes secured by lease revenues as a mechanism for financing City of San José public improvements such as the offsite parking garage for City Hall, Phase II improvements of the

City's Central Service Yard, non-construction costs for technology, furniture, equipment and relocation services at City Hall, and procuring the consolidated utility billing system. The amount of commercial paper notes outstanding increased from $80.3 million on June 30, 2007 to $83.8 million on June 30, 2008, a net increase of $3.6 million or 4.4 percent primarily due to the issuance of commercial paper notes for capital improvements at the City's HP Pavilion.

Total other financing sources increased by $27.7 million or 94.2 percent to $57.1 million. This increase is primarily due to increases in transfers-in of $9.5 million for debt service payments and a decrease of $13.7 million in commercial paper proceeds transfers-out for capital projects and operations.

Proprietary funds

The City's proprietary funds provide the same type of information found in the government-wide financial statements for business-type activities, but in more detail. At June 30, 2008, the unrestricted net assets were $77.6 million for the Norman Y. Mineta San José International Airport, $175.2 million for the Wastewater Treatment System, $8.1 million for the Municipal Water System and $20.7 million for the Parking System. Net assets for proprietary funds grew from $1.249 billion at June 30, 2007 to $1.265 billion at June 30, 2008, an increase of $16.0 million or 1.3 percent. Other aspects of proprietary fund activities are discussed in the business-type activities section above.

GENERAL FUND BUDGETARY HIGHLIGHTS

The City of San José charter requires staff to submit operating and capital budgets to the City Council prior to the beginning of a new fiscal year that begins each July 1 and ends on the following June 30. Council approved the 2008-09 budgets in June 2008. The City is in the second half of its *Decade of Investment*, which is transforming much of the City's infrastructure. Major improvements continue in the City's parks, community centers, libraries and public safety facilities and as a result, the City is continuing to dedicate significant resources towards addressing critical service and infrastructure needs in the 2008-09 budgets.

During the fiscal year ended June 30, 2008, there was a $20.6 million increase in budgeted revenues between the original and final amended operating budget for the General Fund. Over half of the increase was due to increases in property tax collections, Comcast's public, educational and government access capital funding obligation, the sale of surplus land in the amount of $2.4 million, and interest earnings reflecting higher cash balances.

In addition, there was a $63.6 million increase in appropriations between the original and final amended operating budget for the General Fund. Following are the main components of the increase:

- A supplemental appropriation of $38.1 million to Public Safety that included increases related to salary and benefits resulting from the award of interest arbitration between the City and the International Association of Firefighters, Local 230, including a retroactive payout for the period 2005-06 through 2006-07, and increases related to the 2006 and 2007 Super Urban Areas Security Initiative (UASI) budgets to support operational costs related to Orange Alerts (terrorists threat level) at the Norman Y. Mineta San José International Airport. These costs were reimbursed to the General Fund by a transfer from the Airport.
- A supplemental appropriation of $16.6 million for Capital Maintenance that included increases related to street maintenance repairs and resurfacing, and site clean-up and restoration costs for Watson Park, a 35-acre park, due to the presence of burn ash and dump debris from approximately 70 years earlier.

Actual budgetary basis expenditures of $740.9 million were $89.7 million less than the amended budget and $26.1 million less than the original budget. Savings were experienced over all expenditure categories.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

The City of San José's investment in capital assets, net of accumulated depreciation, for its governmental and business-type activities together amounted to $9.429 billion at June 30, 2008. This investment includes land, infrastructure, structures and improvements, vehicles, equipment, intangible assets, and construction-in-progress. The City of San José's decision to depreciate infrastructure capital assets results in recording a large non-cash depreciation expense each year that offsets additions to capital assets. The result of the new additions less depreciation expense during 2007-08 yielded a $146.2 million decrease in governmental activities net capital assets offset by a $247.8 million increase in business-type activities net capital assets resulting in an overall increase of $101.6 million or 1.1 percent in net capital asset balances between June 30, 2007 and June 30, 2008.

Total construction-in-progress increased $61.5 million or 8.8 percent from $695.2 million at June 30, 2007 to $756.7 million at June 30, 2008. The governmental activities' portion of construction-in-progress decreased $156.4 million. In contrast, business-type activities contributed a net increase of $217.9 million to construction-in–progress due to the on-going Airport expansion ($273.2 million), offset by decreases to the Municipal Water System ($0.6 million) and the Wastewater Systems ($54.7 million) capital projects. Outstanding commitments related to construction-in-progress at June 30, 2008 totaled $139.4 million and $523.2 million for governmental and business-type activities, respectively.

The City of San José records infrastructure assets at historical cost in the government-wide financial statements and depreciates assets from acquisition date to the end of the current fiscal year as required by GASB Statement No. 34. For governmental fund financial statements recording purposes, capital asset purchases are recorded as expenditures, rather than capitalizing and recording related depreciation. Capital assets, net of depreciation, for governmental and business-type activities in the government-wide financial statements are presented below to illustrate changes between June 30, 2007 and June 30, 2008 (in thousands):

		Governmental activities		Business-type activities		Total		Increase/ (Decrease)
		2008	2007	2008	2007	2008	2007	Percent of Change
Land	$	559,825	550,416	134,926	134,926	694,751	685,342	1.4%
Construction in progress		140,489	296,914	616,188	398,252	756,677	695,166	8.8%
Buildings		997,119	822,140	328,641	281,334	1,325,760	1,103,474	20.1%
Improvements, other than buildings		121,308	33,557	490,012	506,219	611,320	539,776	13.3%
Infrastructure		5,949,391	6,211,589	-	-	5,949,391	6,211,589	-4.2%
Furniture and fixtures, vehicles, equipment		37,364	36,813	41,214	41,657	78,578	78,470	0.1%
Intangible assets		-	-	7,577	7,932	7,577	7,932	-4.5%
Property under capital leases		1,267	1,491	3,253	3,708	4,520	5,199	-13.1%
Total capital assets	$	7,806,763	7,952,920	1,621,811	1,374,028	9,428,574	9,326,948	1.1%

Additional information about the City's capital assets can be found in Note III.D to the financial statements.

General Fund Bonded Debt Limit

The City of San José Charter limits bonded indebtedness for General Obligation bonds to 15 percent of the total assessed valuation of all real and personal property within the City. The total assessed value on the City's 2007-08 tax roll was $122.634 billion, which results in a net total debt capacity of $17.866 billion. As of June 30, 2008, the City had $528.6 million of General Obligation bonds outstanding.

General Obligation Bond Rating

In May 2008, Standard & Poor's, one of the three national credit rating agencies, raised the City's general obligation bond rating to the highest level of AAA and Moody's Investors Service and Fitch Ratings reaffirmed the City's high ratings of Aa1 and AA+, respectively, ranking it higher than the State of California and all other California large cities.

Outstanding Debt

The City's debt service obligations include general obligation bonds, revenue bonds, lease revenue bonds, special assessment bonds, and Redevelopment Agency tax allocation bonds.

At June 30, 2008, the City had $3.603 billion of gross outstanding long-term debt related to governmental activities and $1.176 billion related to business-type activities, for a total of $4.779 billion. These amounts for the fiscal year ended June 30, 2007 were $3.433 billion for governmental activities and $608.3 million for business-type activities, for a total of $4.041 billion.

The table below identifies the net changes in each category (in thousands):

		As of June 30 2008	As of June 30 2007	Net Change
Governmental Activities				
General obligation bonds	$	528,565	510,710	17,855
HUD Section 108 loan		24,876	25,436	(560)
Lease revenue and revenue bonds		629,324	641,551	(12,227)
Special assessments		68,151	71,580	(3,429)
Redevelopment Agency		2,352,465	2,183,295	169,170
Sub-total		3,603,381	3,432,572	170,809
Business-Type Activities				
Revenue bonds		1,133,690	562,730	570,960
State of CA-Revolving Fund Loan		41,952	45,585	(3,633)
Sub-total		1,175,642	608,315	567,327
Total:	$	4,779,023	4,040,887	738,136

Additional information about the City's long-term obligations appears in Note III.F. of the notes to the financial statements.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGET AND RATES

- Stagnant growth is projected in fiscal year 2008-09 for the City's economically sensitive revenues including Property Tax, Construction and Conveyance Taxes, and Sales Tax, due to the declining housing market, faltering financial sectors, and rising energy costs. It is important to note, however, that only about half of the City's revenue categories are tied directly to the performance of the economy. The remaining areas, while impacted by overall economic performance, are driven by other factors. For instance, growth in the Utility Tax and Franchise fee categories is typically more heavily impacted by rate changes than economic growth.

- The 2008-09 budget focuses on City Council priorities, directing resources toward essential services such as public safety, basic infrastructure requirements, economic development opportunities, and maintaining the City's strong commitment to neighborhoods. To meet these priorities, the City Council approved a balanced General Fund budget for fiscal year 2008-09, closing a funding gap of approximately $29.6 million primarily with ongoing reductions and fee increases combined with the strategic use of reserves and other one-time revenue sources.

- Effective for fiscal years beginning after December 15, 2006, the Governmental Accounting Standards Board (GASB) Statement No. 45 requires governments to report the amount of unfunded liabilities for postemployment benefits other than pensions (such as medical benefits). GASB 45 also encourages governments to fund these liabilities over the long-term. The 2008-09 budget includes $1.9 million in funding to begin addressing the City's share of the unfunded liability associated with postemployment benefits, and City staff is actively researching longer term strategies to address this liability.

- The 2008-09 budget recommends rate increases of 30.0 percent for the Storm Sewer Service and Use Charge, 4.5 percent for Recycle Plus single family dwellings, and 8.8 percent for the Municipal Water System in order to maintain a reliable utility infrastructure.

- San José's average unemployment rate for calendar year 2007 increased by less than 1.0 percent over the prior year average, but the City's current rate is still lower than the average unemployment rate for the State. The City's average unemployment rate for calendar year 2007 was 5.3 percent, which is slightly lower than the statewide average of 5.4 percent.

All of these factors were considered in preparing the City's budget for 2008-09.

The recent turmoil in the financial market has been unprecedented. In September 2008, the U.S. Treasury placed government sponsored enterprises Fannie Mae (Federal National Mortgage Association) and Freddie Mac (Federal Home Loan Mortgage Corporation) into conservatorship and committed to provide as much as $100 billion to each company to backstop any shortfalls in capital through 2009, which protected the principal and interest payments on their debt (bonds issued). In addition, the federal government recently assumed control of American International Group Inc. (AIG), the largest insurance company in the U. S.; Lehman Brothers Holdings Inc., the 4th largest investment bank in the U.S. filed for bankruptcy; and Washington Mutual Inc. was seized by government regulators and its branches and assets sold to JPMorgan Chase & Co. On October 3, 2008, the President of the United States signed into law the $700 billion Emergency Economic Stabilization Act of 2008 in an effort to address the economic crisis. Further information regarding the changes in the economic environment and its impact to the City is contained in the Subsequent Events footnote (D.2) to the Basic Financial Statements.

REQUEST FOR INFORMATION

This financial report is designed to provide our residents, taxpayers, customers, investors, and creditors with a general overview of the City's finances. Questions concerning any of the information provided in his report or requests for additional financial information should be addressed to the Director of Finance, 200 E. Santa Clara Street, San José, CA 95113.

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CITY OF SAN JOSE
CAPITAL OF SILICON VALLEY

Basic Financial Statements

CITY OF SAN JOSE
CAPITAL OF SILICON VALLEY

City of San José
Statement of Net Assets
June 30, 2008
($000's)

		Governmental Activities	Business-Type Activities	Total
ASSETS				
Equity in pooled cash and investments	$	819,896	297,268	1,117,164
Other cash and investments		6	-	6
Receivables (net of allowances for uncollectibles)		176,605	11,876	188,481
Due from outside agencies		3,141	356	3,497
Internal balances		(9,377)	9,377	-
Inventories		1,577	1,273	2,850
Loans receivable (net)		319,385	250	319,635
Advances and deposits		546	8,101	8,647
Other assets		22,504	4,868	27,372
Restricted assets:				
Equity in pooled cash and investments		78,712	166,784	245,496
Other cash and investments		485,270	585,293	1,070,563
Receivables (net of allowances for uncollectibles)		-	13,354	13,354
Deferred bond issuance costs (net of accumulated amortization)		53,641	13,321	66,962
Capital assets (net of accumulated depreciation):				
Nondepreciable		700,314	751,114	1,451,428
Depreciable		7,106,449	870,697	7,977,146
Total assets		9,758,669	2,733,932	12,492,601
LIABILITIES				
Accounts payable		59,715	59,263	118,978
Accrued liabilities		31,122	2,450	33,572
Interest payable		52,872	12,990	65,862
Due to outside agencies		16,819	-	16,819
Short term notes payable		83,829	186,190	270,019
Unearned revenue		21,984	3,351	25,335
Advances, deposits, and reimbursable credits		20,265	4,374	24,639
Other liabilities		15,083	330	15,413
Noncurrent obligations:				
Due within one year		127,313	30,218	157,531
Due in more than one year		3,801,750	1,169,896	4,971,646
Total liabilities		4,230,752	1,469,062	5,699,814
NET ASSETS				
Invested in capital assets, net of related debt		4,769,191	823,223	5,592,414
Restricted for:				
Debt service		75,956	48,110	124,066
Capital projects		317,678	112,043	429,721
Community services		265,837	-	265,837
Public safety		3,392	-	3,392
Unrestricted		95,863	281,494	377,357
Total net assets	$	5,527,917	1,264,870	6,792,787

The notes to the financial statements are an integral part of this statement.

City of San José
Statement of Activities
For the Year Ended June 30, 2008
($000's)

Functions/Programs	Expenses	Program Revenues: Fees, Fines, and Charges for Services	Program Revenues: Operating Grants and Contributions	Program Revenues: Capital Grants and Contributions	Net (Expense) Revenue and Changes in Net Assets: Governmental Activities	Net (Expense) Revenue and Changes in Net Assets: Business -Type Activities	Net (Expense) Revenue and Changes in Net Assets: Total
Governmental activities:							
General government	$ 142,886	32,585	36	-	(110,265)	-	(110,265)
Public safety	476,570	45,845	15,618	-	(415,107)	-	(415,107)
Capital maintenance	569,636	37,580	38,448	48,075	(445,533)	-	(445,533)
Community services	211,511	88,050	40,255	-	(83,206)	-	(83,206)
Sanitation	113,525	121,793	-	-	8,268	-	8,268
Unallocated interest and fiscal charges	170,852	-	-	-	(170,852)	-	(170,852)
Total governmental activities	**1,684,980**	**325,853**	**94,357**	**48,075**	**(1,216,695)**	**-**	**(1,216,695)**
Business -Type activities:							
Norman Y. Mineta San José International Airport	153,927	138,532	8,444	4,970	-	(1,981)	(1,981)
Wastewater Treatment System	134,882	129,568	-	4,003	-	(1,311)	(1,311)
Municipal Water System	26,017	24,154	-	189	-	(1,674)	(1,674)
Parking System	10,127	11,226	-	-	-	1,099	1,099
Total business-type activities	**324,953**	**303,480**	**8,444**	**9,162**	**-**	**(3,867)**	**(3,867)**
Total	**$ 2,009,933**	**629,333**	**102,801**	**57,237**	**(1,216,695)**	**(3,867)**	**(1,220,562)**

	Governmental Activities	Business -Type Activities	Total
General revenues:			
Taxes:			
Property and other taxes	495,731	-	495,731
Utility	82,255	-	82,255
Franchise	41,064	-	41,064
Transient occupancy	23,900	-	23,900
Sales taxes shared revenue (unrestricted)	149,500	-	149,500
State of California in-lieu (unrestricted)	9,244	-	9,244
Business license tax	39,901	-	39,901
Unrestricted interest and investment earnings	65,721	29,232	94,953
Other revenue	53,420	-	53,420
Transfers	9,383	(9,383)	-
Total general revenues and transfers	**970,119**	**19,849**	**989,968**
Change in net assets	**(246,576)**	**15,982**	**(230,594)**
Net assets - beginning	**5,774,493**	**1,248,888**	**7,023,381**
Net assets - ending	**$ 5,527,917**	**1,264,870**	**6,792,787**

The notes to the financial statements are an integral part of this statement.

City of San José
Balance Sheet
Governmental Funds
June 30, 2008
($000's)

		General Fund	Redevelopment Agency	Housing Activities
ASSETS				
Equity in pooled cash and investments held in City Treasury	$	246,586	156,575	41,521
Other cash and investments		-	-	-
Receivables (net of allowance for uncollectibles)		57,829	668	10,245
Due from outside agencies		2,766	-	51
Due from other funds		19,165	1,468	8
Inventories		-	-	-
Loans receivable (net)		2,141	42,223	268,258
Advances and deposits		13	60	-
Restricted assets:				
Equity in pooled cash and investments held in City Treasury		1,024	-	11,008
Other cash and investments		-	97,357	-
Advances to other funds		3,338	830	-
Other assets		347	-	21,083
Total assets	$	333,209	299,181	352,174
LIABILITIES AND FUND BALANCES				
Liabilities:				
Accounts payable	$	10,719	5,178	2,829
Accrued salaries, wages, and payroll taxes		25,862	477	358
Due to other funds		1,169	3,459	80
Due to other agencies		529	23,790	-
Short term notes payable		-	-	-
Deferred revenue		7,484	42,381	25,434
Advances, deposits, and reimbursable credits		7	1,824	-
Advances from other funds		250	14,912	580
Other liabilities		10,056	-	-
Total liabilities		56,076	92,021	29,281
Fund balances:				
Reserved for:				
Encumbrances		41,648	26,921	36,587
Noncurrent advances, loans and other assets		6,863	4,770	272,106
Debt service		-	92,921	-
Restricted cash commitments		-	-	3
Unreserved reported in:				
General fund		228,622	-	-
Special revenue funds		-	-	14,197
Debt service funds		-	-	-
Capital projects funds		-	82,548	-
Total fund balances		277,133	207,160	322,893
Total liabilities and fund balances	$	333,209	299,181	352,174

The notes to the financial statements are an integral part of this statement.

Special Assessment Districts	San José Financing Authority Debt Service	Nonmajor Governmental Funds	Total Governmental Funds
-	2	370,088	814,772
-		6	6
68,235	-	39,594	176,571
32	-	292	3,141
-	-	23,845	44,486
-	-	1,577	1,577
-		6,763	319,385
309	-	164	546
28,928	608	37,144	78,712
10,974	55,723	321,216	485,270
-	-	8,112	12,280
-	-	1,074	22,504
108,478	56,333	809,875	1,959,250
-	139	40,838	59,703
8	-	3,988	30,693
-	-	40,201	44,909
-	-	-	24,319
-	83,829	-	83,829
68,455	-	11,702	155,456
4,009	-	14,425	20,265
-	3,338	2,154	21,234
-	-	5,027	15,083
72,472	87,306	118,335	455,491
355	94	183,182	288,787
5	-	17,577	301,321
21,633	-	38,859	153,413
-	-	395	398
-	-	-	228,622
-	-	284,881	299,078
-	(31,067)	166,646	135,579
14,013	-	-	96,561
36,006	(30,973)	691,540	1,503,759
108,478	56,333	809,875	1,959,250

City of San José

Reconciliation of the Governmental Funds Balance Sheet
to the Statement of Net Assets
June 30, 2008
($000's)

Total fund balances-governmental funds (Page 22)		$ 1,503,759
Amounts reported for governmental activities in the statement of net assets are different because:		
Capital assets used in governmental activities are not financial resources and therefore are not reported in the funds. These assets consist of:		
Land	559,825	
Infrastructure assets	11,278,414	
Other capital assets	1,677,364	
Accumulated depreciation	(5,708,840)	
Total capital assets		7,806,763
Interest payable on long-term debt does not require the use of current financial resources and, therefore, interest payable is generally not accrued as a liability in the balance sheet of governmental funds.		(52,872)
Bond issuance costs are expended in governmental funds when paid, however, are capitalized and amortized over the life of the corresponding bonds for purposes of the statement of net assets. Deferred charges, net of amortization		53,641
Special Assessments are reported as revenue when levied in government-wide financial statements. In governmental funds, these assessments are reported as deferred revenue (a liability) since they are not available.		68,151
Long-term receivables are not available to pay for current period expenditures and, therefore, are deferred on the modified accrual basis.		65,321
The Public Works Program Support Internal Service fund is used by management to charge its costs to individual funds. The assets and liabilities of the internal service fund is included in governmental activities in the Statement of Net Assets.		2,358
Long-term liabilities are not due and payable in the current period and therefore are not reported in the funds. Those liabilities consist of:		
Bonds and notes payable	(3,609,501)	
Accreted interest on capital appreciation bonds	(2,083)	
Compensated absences	(91,765)	
Claims and judgments	(138,838)	
Other	(77,017)	
Total long-term liabilities		(3,919,204)
Net assets of governmental activities (Page 20)		$ 5,527,917

The notes to the financial statements are an integral part of this statement.

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CITY OF SAN JOSE
CAPITAL OF SILICON VALLEY

City of San José
Statement of Revenues, Expenditures
and Changes in Fund Balances
Governmental Funds
For the Year Ended June 30, 2008
($000's)

		General Fund	Redevelopment Agency	Housing Activities
REVENUES				
Taxes and special assessments	$	499,843	184,942	-
Licenses, permits, and fines		89,656	-	-
Intergovernmental		12,762	1,560	11,313
Charges for current services		30,533	-	-
Rent		-	1,834	6
Investment income		26,152	9,536	18,660
Other revenue		35,462	12,304	9,822
Total revenues		694,408	210,176	39,801
EXPENDITURES				
Current:				
General government		86,907	17,747	-
Public safety		416,255	-	-
Capital maintenance		50,678	84,266	44
Community services		141,878	-	1,620
Sanitation		1,896	-	-
Capital outlay		1,469	45,330	-
Debt service:				
Principal		-	42,385	-
Interest and fiscal charges		-	103,795	-
Bond issuance costs		-	3,694	-
Current refunding escrow		-	-	-
Total expenditures		699,083	297,217	1,664
Excess (deficiency) of revenues over (under) expenditures		(4,675)	(87,041)	38,137
OTHER FINANCING SOURCES (USES)				
Bonds issued		-	212,930	-
Refunding bonds issued		-	-	-
Premiums on bonds		-	1,129	-
Payment to refunded bond escrow agent		-	-	-
Loan proceeds		374	-	-
Transfers in		39,192	23,142	50,843
Transfers out		(38,355)	(65,010)	(19,572)
Total other financing sources (uses)		1,211	172,191	31,271
Net change in fund balances		(3,464)	85,150	69,408
Fund balances - beginning		280,597	122,010	253,485
Fund balances - ending	$	277,133	207,160	322,893

The notes to the financial statements are an integral part of this statement.

Special Assessment Districts	San José Financing Authority Debt Service	Nonmajor Governmental Funds	Total Governmental Funds
6,335	-	136,411	827,531
-	-	-	89,656
-	-	71,295	96,930
-	-	265,747	296,280
-	-	11,949	13,789
1,741	2,262	27,787	86,138
726	27	25,028	83,369
8,802	2,289	538,217	1,493,693
-	-	134,093	238,747
-	-	2,614	418,869
620	-	112,595	248,203
15	-	48,028	191,541
-	-	110,069	111,965
-	-	124,776	171,575
3,429	9,420	16,387	71,621
3,922	35,978	24,142	167,837
-	613	411	4,718
-	12,992	-	12,992
7,986	59,003	573,115	1,638,068
816	(56,714)	(34,898)	(144,375)
-		33,100	246,030
-	125,500	-	125,500
-	-	516	1,645
-	(116,908)	-	(116,908)
-	-	-	374
-	57,901	68,129	239,207
-	(9,353)	(97,534)	(229,824)
-	57,140	4,211	266,024
816	426	(30,687)	121,649
35,190	(31,399)	722,227	1,382,110
36,006	(30,973)	691,540	1,503,759

City of San José

Reconciliation of the Changes in Fund Balances of Governmental Funds
to the Statement of Activities
For the Year Ended June 30, 2008
($000's)

Net change in fund balances--total governmental funds (Page 26)		$ 121,649
Amounts reported for governmental activities in the statement of activities are different because:		
Capital outlays are reported as expenditures in governmental funds. However, in the statement of activities, the cost of capital assets is allocated over their estimated useful lives as depreciation expense. In the current period, these amounts are:		
Capital outlay	171,575	
Depreciation expense	(345,615)	
Excess of depreciation expense over capital outlay		(174,040)
The net effect of various miscellaneous transactions involving capital assets (i.e. sales, retirements, trade-ins, donations)		
Donated assets	31,896	
Disposal of assets	(4,013)	
		27,883
Bond issuance costs are expended in governmental funds when paid, however, are capitalized and amortized over the life of the corresponding bonds for the purposes of the statement of activities.		
Bond issuance costs	4,718	
Amortization of bond issuance costs	(4,012)	
Total bond issuance costs, net of amortization		706
Repayment of long-term obligation principal is reported as an expenditure in governmental funds and, thus, has the effect of reducing fund balance because current financial resources have been used. For the government-wide statements, however, the principal payments reduce the liabilities in the statement of net assets and do not result in an expense in the statement of activities. The City's long-term obligations were reduced because principal payments were made to bondholders and HUD.		201,521
Accrued interest expense on long-term debt is reported in the government-wide statement of activities, but does not require the use of current financial resources. Amortization of bond premiums, discounts and deferred amounts on refunding should be expensed as a component of interest expense on the statement of activities. This amount represents the net accrued interest expense and the amortization of bond premiums, discounts and deferred amounts on refunding not reported in governmental funds.		
Accrued interest on capital appreciation bonds	(218)	
Premium on bonds issued	(1,645)	
Increase in accrued interest expense	(3,823)	
Amortization of deferred amounts, premiums and discounts	258	
Deferred amounts on bonds issued	1,080	
Total net interest expense and amortization of discount/premium		(4,348)
Bond and loan proceeds provide current financial resources to governmental funds, however, issuing debt increases long-term liabilities in the statement of net assets.		(371,904)
Because some revenues will not be collected for several months after the City's fiscal year ends, they are not considered "available" revenue and are deferred in the governmental funds. Deferred revenues increased by this amount this year.		922
Some items reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in governmental funds. These activities consist of:		
Net decrease in accrued landfill postclosure costs	465	
Net increase in net pension obligation and OPEB obligation	(63,445)	
Net increase in vacation, sick leave, and compensatory time	(1,774)	
Net decrease in estimated liability for self-insurance	4,319	
Net decrease in other accrued liabilities	11,119	
Net decrease in arbitrage liability	768	
Total additional expenditures		(48,548)
The net expenses of the Public Works Program Support Internal Service fund is reported with the governmental activities		(417)
Change in net assets of governmental activities (Page 21)		$ (246,576)

The notes to the financial statements are an integral part of this statement.

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City of San José
Statement of Fund Net Assets
Proprietary Funds
June 30, 2008
($000's)

	Norman Y. Mineta San José International Airport	Wastewater Treatment System	Municipal Water System	Parking System	Totals	Public Works Program Support Internal Service Fund
ASSETS						
Current assets:						
Equity in pooled cash and investments held in City Treasury	$ 48,637	220,991	12,634	15,006	297,268	5,124
Receivables (net of allowance for uncollectibles)	2,713	5,869	3,096	198	11,876	34
Due from outside agencies	-	356	-	-	356	-
Due from other funds	14	1,409	-	-	1,423	-
Inventories	-	1,273	-	-	1,273	-
Total unrestricted current assets	51,364	229,898	15,730	15,204	312,196	5,158
Restricted assets:						
Equity in pooled cash and investments held in City Treasury	146,042	19,159	-	1,583	166,784	-
Other cash and investments	585,114	179	-	-	585,293	-
Receivables (net of allowances for uncollectibles)	13,354	-	-	-	13,354	-
Prepaid expenses, advances and deposits	4,830	-	-	38	4,868	-
Total restricted current assets	749,340	19,338	-	1,621	770,299	-
Total current assets	800,704	249,236	15,730	16,825	1,082,495	5,158
Noncurrent assets:						
Deferred bond issuance costs (net of accumulated amortization)	12,569	752	-	-	13,321	-
Loan receivable	250	-	-	-	250	-
Advances and deposits	8,101	-	-	-	8,101	-
Advances to other funds	-	4,850	-	6,800	11,650	-
Capital assets (net of accumulated depreciation):						
Nondepreciable	585,129	145,499	1,577	18,909	751,114	-
Depreciable	343,642	403,821	72,756	50,478	870,697	-
Total noncurrent assets	949,691	554,922	74,333	76,187	1,655,133	-
Total assets	1,750,395	804,158	90,063	93,012	2,737,628	5,158

The notes to the financial statements are an integral part of this statement.

City of San José
Statement of Fund Net Assets
Proprietary Funds
June 30, 2008
($000's)

	Norman Y. Mineta San José International Airport	Wastewater Treatment System	Municipal Water System	Parking System	Totals	Public Works Program Support Internal Service Fund
LIABILITIES						
Current liabilities:						
Accounts payable	$ 3,253	7,241	1,885	908	13,287	12
Accrued liabilities	65	2,145	166	74	2,450	429
Interest payable	-	431	-	-	431	-
Due to other funds	-	-	1,000	-	1,000	-
Accrued vacation, sick leave and compensatory time	266	5,044	239	176	5,725	2,359
Estimated liability for self-insurance	-	1,283	179	1	1,463	-
Loans payable	-	3,699	-	-	3,699	-
Total current liabilities unrestricted	3,584	19,843	3,469	1,159	28,055	2,800
Current liabilities payable from restricted assets:						
Accounts payable and accrued liabilities	45,976	-	-	-	45,976	-
Interest payable	12,318	241	-	-	12,559	-
Accrued vacation, sick leave and compensatory time	3,670	-	-	-	3,670	-
Estimated liability for self-insurance	560	-	-	-	560	-
Advances and deposits payable	873	-	-	-	873	-
Deferred revenue	3,351	-	-	-	3,351	-
Short term notes payable	186,190	-	-	-	186,190	-
Current portion of bonds payable	10,780	4,321	-	-	15,101	-
Total current liabilities payable from restricted assets	263,718	4,562	-	-	268,280	-
Total current liabilities	267,302	24,405	3,469	1,159	296,335	2,800
Noncurrent liabilities:						
Estimated liability for self-insurance	2,801	3,901	-	-	6,702	-
Advances from other funds	-	-	2,696	-	2,696	-
Advance contributions from participating agencies	-	2,397	-	-	2,397	-
Advances, deposits and reimbursable credits	-	-	1,104	-	1,104	-
Loans payable	-	38,253	-	-	38,253	-
Bonds payable (net of discount and deferred loss on premium/refunding)	1,046,606	67,340	-	-	1,113,946	-
Other liabilities	4,997	5,772	404	152	11,325	-
Total noncurrent liabilities	1,054,404	117,663	4,204	152	1,176,423	-
Total liabilities	1,321,706	142,068	7,673	1,311	1,472,758	2,800
NET ASSETS						
Invested in capital assets, net of related debt	237,033	442,470	74,333	69,387	823,223	-
Restricted for debt service	46,527	-	-	1,583	48,110	-
Restricted for capital projects	67,578	44,465	-	-	112,043	-
Unrestricted	77,551	175,155	8,057	20,731	281,494	2,358
Total net assets	$ 428,689	662,090	82,390	91,701	1,264,870	2,358

City of San José
Statement of Revenues, Expenses, and Changes in Fund Net Assets
Proprietary Funds
For the Year Ended June 30, 2008
($000's)

		Norman Y. Mineta San José International Airport	Wastewater Treatment System	Municipal Water System	Parking System	Totals	Public Works Program Support Internal Service Fund
OPERATING REVENUES							
Charges for services	$	50,021	102,237	24,034	11,128	187,420	15,397
Rentals and concessions		58,451	2,387	-	-	60,838	-
Customer transportation fees		6,351	-	-	-	6,351	-
Service connection, engineering and inspection		-	2,959	-	-	2,959	-
Contributions		-	10,916	-	-	10,916	-
Other		63	6,627	-	-	6,690	-
Total operating revenues		114,886	125,126	24,034	11,128	275,174	15,397
OPERATING EXPENSES							
Operations and maintenance		86,157	75,991	22,210	4,202	188,560	15,973
General and administrative		32,878	29,449	1,047	3,667	67,041	-
Depreciation and amortization		23,155	25,256	2,592	2,027	53,030	-
Materials and supplies		-	339	-	231	570	-
Total operating expenses		142,190	131,035	25,849	10,127	309,201	15,973
Operating income (loss)		(27,304)	(5,909)	(1,815)	1,001	(34,027)	(576)
NONOPERATING REVENUES (EXPENSES)							
Passenger facility charges		21,224	-	-	-	21,224	-
Operating grants		8,444	-	-	-	8,444	-
Investment income		15,446	12,209	738	839	29,232	159
Land and building rental		-	42	-	-	42	-
Interest expense		(11,737)	(3,543)	(168)	-	(15,448)	-
Contributions refunded to participating agencies		-	(298)	-	-	(298)	-
Loss on disposal of capital assets		-	(6)	-	-	(6)	-
Other revenues		2,422	4,400	120	98	7,040	-
Net nonoperating revenues (expenses)		35,799	12,804	690	937	50,230	159
Income (loss) before capital contributions and transfers		8,495	6,895	(1,125)	1,938	16,203	(417)
Capital contributions		4,970	4,003	189	-	9,162	-
Transfers in		810	122	-	29	961	-
Transfers out		(110)	(7,492)	(1,335)	(1,407)	(10,344)	-
Changes in net assets		14,165	3,528	(2,271)	560	15,982	(417)
Net assets - beginning		414,524	658,562	84,661	91,141	1,248,888	2,775
Net assets - ending	$	428,689	662,090	82,390	91,701	1,264,870	2,358

The notes to the financial statements are an integral part of this statement.

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CITY OF SAN JOSE
CAPITAL OF SILICON VALLEY

City of San José
Statement of Cash Flows
Proprietary Funds
For the Year Ended June 30, 2008
($000's)

		Norman Y. Mineta San José International Airport	Wastewater Treatment System	Municipal Water System	Parking System	Totals	Public Works Program Support Internal Service Fund
CASH FLOWS FROM OPERATING ACTIVITIES							
Receipts from customers and users	$	116,325	112,791	23,909	12,325	265,350	15,397
Payments to suppliers		(76,854)	(44,566)	(18,587)	(5,760)	(145,767)	(2,277)
Payments to employees		(35,968)	(52,642)	(4,023)	(1,872)	(94,505)	(11,262)
Other receipts		2,670	11,930	-	-	14,600	-
Net cash provided by operating activities		6,173	27,513	1,299	4,693	39,678	1,858
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES							
Transfer from other funds		810	122	-	29	961	-
Transfer to other funds		(110)	(7,492)	(1,335)	(1,407)	(10,344)	-
Advances (to) from other funds		175	681	(700)	-	156	-
Subsidies from operating grants		8,238	-	-	-	8,238	-
Advances, deposits and credits		(14)	-	(81)	-	(95)	-
Net cash provided by (used in) by noncapital and related financing activities		9,099	(6,689)	(2,116)	(1,378)	(1,084)	-
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES							
Passenger facility charges received		22,961	-	-	-	22,961	-
Proceeds from commercial paper		177,172	-	-	-	177,172	-
Proceeds from issuance of revenue bonds		722,295	-	-	-	722,295	-
Principal payment for commercial paper		(32,406)	-	-	-	(32,406)	-
Subsidies from capital grants		6,004	966	-	-	6,970	-
Acquisition and construction of capital assets		(250,206)	(17,675)	(813)	(895)	(269,589)	-
Principal paid on debt		(9,745)	(7,943)	-	-	(17,688)	-
Payment for redemption of bonds		(140,000)	-	-	-	(140,000)	-
Bond issuance costs		(7,666)	-	-	-	(7,666)	-
Interest paid on debt		(41,502)	(3,405)	-	-	(44,907)	-
Advances, deposits and credits paid		(2,063)	-	-	-	(2,063)	-
Net cash provided by (used in) capital and related financing activities		444,844	(28,057)	(813)	(895)	415,079	-
CASH FLOWS FROM INVESTING ACTIVITIES							
Proceeds from sales and maturities of investments		415,660	-	-	-	415,660	-
Purchase of investments		(961,340)	-	-	-	(961,340)	-
Interest and dividends received		35,750	12,283	753	826	49,612	125
Land and building rentals		-	3,796	-	-	3,796	-
Net cash provided by (used in) investing activities		(509,930)	16,079	753	826	(492,272)	125
Net change in cash and cash equivalents		(49,814)	8,846	(877)	3,246	(38,599)	1,983
Cash and cash equivalents - beginning		244,745	231,483	13,511	13,343	503,082	3,141
Cash and cash equivalents - ending	$	194,931	240,329	12,634	16,589	464,483	5,124

(Continued)

The notes to the financial statements are an integral part of this statement.

City of San José
Statement of Cash Flows
Proprietary Funds
For the Year Ended June 30, 2008
($000's)

		Norman Y. Mineta San José International Airport	Wastewater Treatment System	Municipal Water System	Parking System	Totals	Public Works Program Support Internal Service Fund
Reconciliation of operating income (loss) to net cash provided by operating activities:							
Operating income (loss)	$	(27,304)	(5,909)	(1,815)	1,001	(34,027)	(576)
Adjustments to reconcile operating income (loss) to net cash provided by operating activities:							
Depreciation and amortization		23,155	25,256	2,592	2,027	53,030	-
Other nonoperating revenues		2,422	647	120	98	3,287	-
Decrease (increase) in:							
Accounts receivable		(1,380)	(1,357)	(246)	1,098	(1,885)	-
Due from outside agencies		-	305	-	-	305	-
Inventories		-	8	-	-	8	-
Prepaid expenses		400	-	-	(38)	362	-
Increase (decrease) in:							
Accounts payable and accrued liabilities		1,937	1,687	(25)	340	3,939	75
Accrued vacation, sick leave and compensatory time		493	504	241	21	1,259	2,359
Estimated liability for self-insurance		(509)	600	28	(6)	113	-
Deferred revenues		2,201	-	-	-	2,201	-
Advances and deposits payable		91	-	-	-	91	-
Other liabilities		4,667	5,772	404	152	10,995	-
Total adjustments		33,477	33,422	3,114	3,692	73,705	2,434
Net cash provided by operating activities	$	6,173	27,513	1,299	4,693	39,678	1,858
Reconciliation of cash and cash equivalents to the statement of net assets:							
Equity in pooled cash and investments held in City Treasury							
Unrestricted	$	48,637	220,991	12,634	15,006	297,268	5,124
Restricted		146,042	19,159	-	1,583	166,784	-
Other investments		585,114	179	-	-	585,293	-
Less investments not meeting the definition of cash equivalents		(584,862)	-	-	-	(584,862)	-
	$	194,931	240,329	12,634	16,589	464,483	5,124
Noncash noncapital, capital and related financing activities:							
Loss on disposal of capital assets	$	-	6	-	-	6	-
Acquisition of capital assets on accounts payable and accrued liabilities		40,633	-	-	-	40,633	-
Bond discount/(premium)		3,764	-	-	-	3,764	-
Capitalized interest		14,013	-	-	-	14,013	-
Contributions from developers		-	2,552	189	-	2,741	-

The notes to the financial statements are an integral part of this statement.

City of San José
Statement of Fiduciary Net Assets
Fiduciary Funds
June 30, 2008
($000's)

		Pension Trust Funds	James Lick Private Purpose Trust Fund	Agency Funds
ASSETS				
Equity in pooled cash and investments held in City Treasury	$	-	50	1,960
Investments of retirement plans:				
Investments, excluding securities lending collateral:				
Domestic fixed maturities		1,342,550	-	-
International fixed maturities		147,980	-	-
Domestic equities		1,539,175	-	-
International equities		992,740	-	-
Private equities		121,056	-	-
Derivatives		(454)	-	-
Real estate		329,981	-	-
Cash equivalents and short term investments		75	-	-
Securities lending cash collateral investment pool		571,216	-	-
Total investments		5,044,319	-	-
Other cash and investments		-	32	-
Receivables (net of allowances for uncollectibles):				
Accrued investment income		15,499	1	17
Employee contributions		2,166	-	-
Employer contributions		5,635	-	-
Other		172,644	2	-
Total assets		5,240,263	85	1,977
LIABILITIES				
Due to brokers		324,860	-	-
Securities lending collateral, due to borrowers		571,216	-	-
Accrued salaries, wages and payroll taxes		-	-	
Other liabilities		7,711	-	1,977
Total liabilities		903,787	-	1,977
NET ASSETS				
Held in trust for:				
Employees' pension benefits		4,190,380	-	-
Employees' postemployment healthcare benefits		146,096	-	-
Other purpose		-	85	-
	$	4,336,476	85	-

The notes to the financial statements are an integral part of this statement.

City of San José
Statement of Changes in Fiduciary Net Assets
Fiduciary Funds
For the Year Ended June 30, 2008
($000's)

	Pension Trust Funds	James Lick Private Purpose Trust Fund
ADDITIONS		
Investment income:		
Interest	$ 70,666	20
Dividends	40,005	-
Net rental income	10,551	-
Net change in fair value of plan investments	(327,252)	-
Investment expenses	(18,798)	-
Total investment income (loss)	(224,828)	20
Securities lending activities:		
Securities lending income	32,824	-
Securities lending expenses	(28,553)	-
Total securities lending activities	4,271	-
Contributions:		
Employer	133,507	-
Employees	52,129	-
Total contributions	185,636	
Total additions	(34,921)	20
DEDUCTIONS		
General and administrative	5,219	-
Health insurance	36,170	-
Refunds to terminated employees	1,140	-
Retirement and other benefits paid:		
Death benefits paid	11,729	-
Retirement benefits paid	172,995	-
Total deductions	227,253	-
Change in net assets	(262,174)	20
Net assets - beginning	4,598,650	65
Net assets - ending	$ 4,336,476	85

The notes to the financial statements are an integral part of this statement.

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CITY OF
SAN JOSE
CAPITAL OF SILICON VALLEY

Notes to Basic Financial Statements

June 30, 2008

INDEX TO THE NOTES

I. Summary of Significant Accounting Policies

A. Reporting Entity

The City of San José, California (the "City"), was chartered on March 25, 1850, and has operated under a Council–Manager form of government since 1916. The City has defined its reporting entity in accordance with generally accepted accounting principles ("GAAP") in the United States of America, which provide guidance for determining which governmental activities, organizations, and functions should be included in the reporting entity. In evaluating how to define the City for financial reporting purposes, management has considered all potential component units. The primary criterion for including a potential component unit within the reporting entity is the governing body's financial accountability. A primary government is financially accountable if it appoints a voting majority of a component unit's governing body and it is able to impose its will on the component unit, or if there is a potential for the component unit to provide specific financial benefits to, or impose specific financial burdens on, the primary government. A primary government may also be financially accountable if a component unit is fiscally dependent on the primary government regardless of whether the component unit has a separately elected governing board, a governing board appointed by a higher level of government, or a jointly appointed board. Based upon the application of these criteria, the following is a brief description of each component unit included within the City's reporting entity. All such component units have been "blended" as though they are part of the primary government because the component unit's governing body is substantively the same as the City's primary government, and/or the component units provide services entirely, or almost entirely, to the City or otherwise exclusively, or almost exclusively, benefits the City, even though it does not provide services directly to it.

- **Redevelopment Agency of the City of San José** – The Redevelopment Agency of the City of San José (the "Redevelopment Agency") was created by the City Council with the authority and responsibility for redeveloping and upgrading blighted areas of the City. The members of the City Council are also members of the Redevelopment Agency's Board of Directors and, as such, are authorized to transact business and exercise their power to plan, engineer, and carry out projects of the Redevelopment Agency.

- **Parking Authority of the City of San José** – The Parking Authority of the City of San José (the "Parking Authority") was created by the City Council to provide funding through debt issuance for parking facilities constructed on City-owned land. Such parking facilities are leased to the City. Members of the City Council are also members of the Parking Authority's Board of Directors.

- **San José – Santa Clara Clean Water Financing Authority** – The San José – Santa Clara Clean Water Financing Authority (the "Clean Water Financing Authority") was created pursuant to a Joint Exercise of Powers Agreement between the City of San José and the City of Santa Clara. The purpose was to finance the acquisition of, and additions and improvements to the existing San José – Santa Clara Water Pollution Control Plant (the Plant). The Clean Water Financing Authority is governed by a five-member Board of Directors, three are members of the City Council of the City of San José and two are members of the City Council of the City of Santa Clara. The Clean Water Financing Authority and the cities of San José and Santa Clara subsequently entered into an Improvement Agreement, which requires each city to make base payments that are at least equal to each city's allocable share of debt service requirements of the Clean Water Financing Authority's outstanding revenue bonds.

- **City of San José Financing Authority** – The City of San José Financing Authority (the "Authority") was created by a Joint Exercise of Powers Agreement between the City and the Redevelopment Agency. The Authority was created for the purpose of facilitating the financing of public improvements and facilities within the City and is authorized to issue bonds for this purpose. The Authority is governed by an 11 member Governing Board, which consists of the members of the City Council.

Separate financial reports for the fiscal year ended June 30, 2008, containing additional information and more detailed information regarding financial condition and change in financial position, are available from the City's Director of Finance, 200 East Santa Clara Street; 13th Floor, San José, CA 95113-1905, for the following:

- Federated City Employees' Retirement System (the "System")
- Police and Fire Department Retirement Plan (the "Plan")
- Redevelopment Agency of the City of San José
- Norman Y. Mineta San José International Airport
- San José – Santa Clara Clean Water Financing Authority

B. Financial Statement Presentation

Government-wide Financial Statements. The government-wide financial statements (i.e. the statement of net assets and the statement of activities) display information about the primary government (the "City") and its component units. These statements include the financial activities of the overall government, except for fiduciary activities. Eliminations have been made to minimize the double counting of internal activities. For example, the direct expenses charges based on actual use are not eliminated, whereas indirect expense allocations made in the funds are eliminated. These statements distinguish between the *governmental* and *business-type* activities of the City. Governmental activities, which normally are supported by taxes, intergovernmental revenues and other non-exchange transactions, are reported separately from business-type activities, which rely to a significant extent on fees charged to external parties.

The statement of activities, which is included in the government-wide financial statements, presents a comparison between direct expenses and program revenues for each business-type activity of the City and each function of the City's governmental activities. Direct expenses are those that are specifically associated with a business-type activity or governmental function and; therefore, are clearly identifiable to a particular activity or function. Program revenues include 1) fees, fines and charges paid by the recipients of goods or services offered by the programs, and 2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular program. Revenues that are not classified as program revenues, including all taxes, are instead presented as general revenues.

Fund Financial Statements. The fund financial statements provide information about the City's funds, including its fiduciary funds. Separate statements for each fund category, such as governmental, proprietary and fiduciary, are presented. The emphasis of fund financial statements are on the major governmental and enterprise funds of the City and are reported separately in the accompanying financial statements. All remaining governmental funds are aggregated and reported as non-major funds in the accompanying financial statements.

Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain government functions or activities. A fund is a separate accounting entity with a self-balancing set of accounts.

The City reports the following major governmental funds:

The ***General Fund*** is the City's primary operating fund. It accounts for all revenues and expenditures necessary to carry out basic governmental activities of the City that are not accounted for through other funds.

The ***Redevelopment Agency Fund*** is a capital projects fund that accounts for administrative, operating, low-to-moderate income housing program, debt and construction activities necessary to carry out responsibilities for redeveloping and upgrading blighted areas in the City.

The ***Housing Activities Fund*** is a special revenue fund that accounts for the City's affordable housing activities.

The ***Special Assessment Districts Fund*** is a capital projects fund that accounts for the capital project and debt activities related to debt issued to finance public improvements benefiting properties against which special assessments or special taxes are levied.

The **City of San José Financing Authority Fund** is a debt service fund that accounts for the debt activities related to capital projects funded with Authority debt.

The City reports the following major enterprise funds:

The ***Norman Y. Mineta San José International Airport Fund*** accounts for the activities of the City owned commercial service and general aviation airport.

The ***Wastewater Treatment System Fund*** accounts for the financing, construction and operations of the City's sewer system, the Water Pollution Control Plant (the Plant) and the regional water reclamation program.

The ***Municipal Water System Fund*** accounts for the operations of the five water system operating districts: North San José, Evergreen, Coyote, Edenvale and Alviso.

The ***Parking System Fund*** accounts for the operations of the parking garage facilities, parking lots and parking meters located within the City.

The City reports the following fiduciary fund types:

The ***Pension Trust Funds*** account for the accumulated resources to be used for retirement annuity and postemployment healthcare payments to members of the Federated City Employees' Retirement System (the "System") and the Police and Fire Department Retirement Plan (the "Plan" and collectively, the "Retirement System").

The ***James Lick Private Purpose Trust Fund*** is used to account for resources legally held in trust for use towards the support of the Eastfield Home of Benevolence (orphanage). All resources of the fund, including any earnings on invested resources, are used to support the organization's activities.

The ***Agency Funds*** account for assets held by the City in a custodial capacity on behalf of the San José Arena and the Health Care Financing Administration.

The City reports the following internal service fund:

The ***Public Works Program Support Fund*** is used to account for Public Works Department administrative services provided to citywide capital programs and certain other Public Works operating divisions on a cost reimbursement basis.

C. Measurement Focus and Basis of Accounting

The basis of accounting determines when transactions are reported on the financial statements. The government-wide, proprietary and fiduciary funds (excluding agency funds) financial statements are reported using the economic resources measurement focus. The government-wide, proprietary fund and trust funds financial statements are reported using the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded at the time liabilities are incurred, regardless of when the related cash flows take place. Non-exchange transactions, in which the City gives (or receives) value without directly receiving (or giving) equal value in exchange, include property and sales taxes, grants, entitlements and donations. On an accrual basis, revenue from property taxes is recognized in the fiscal year for which the taxes are levied. Revenues from sales and use, transient occupancy and utility user tax are recognized when the underlying transactions take place. Revenues from grants, entitlements and donations are recognized in the fiscal year in which all eligibility requirements have been satisfied.

Governmental funds are reported using the current financial resources measurement focus. This focus is on the determination of, and changes in financial resources, and generally only current assets and current liabilities are included in the balance sheet. These funds use the modified accrual basis of accounting, whereby revenues are recognized in the accounting period in which they become both measurable and available to finance expenditures of the fiscal period. For this purpose, the City considers revenues as available if they are collected within sixty days of the end of the current fiscal period. Expenditures are generally recorded when a liability is incurred. However, principal and interest on long-term debt and certain estimated liabilities, such as compensated absences and self-insurance claims, are recorded only when payment is due.

In governmental funds, revenues from taxes, licenses, franchise taxes, interest, certain state and federal grants and charges for services associated with the current fiscal period are all considered to be susceptible to accrual and so have been recognized as revenues in the current period. All other revenue items are considered measurable and available only when cash is received by the City.

Proprietary funds distinguish between operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues of the City's enterprise funds are charges to customers for sales and services. Operating expenses for enterprise funds include the cost of sales and services, administrative expenses and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

Under the terms of grant agreements, the City funds certain programs by a combination of specific cost-reimbursement grants, categorical block grants and general revenues. Thus, when program expenses are incurred, there are both restricted and unrestricted net assets available to finance the program. It is the City's policy to first apply restricted cost-reimbursement grant resources to such programs, followed by restricted categorical block grants, and then by unrestricted general revenues.

All business-type activities and enterprise funds of the City follow FASB Statements and Interpretations issued on or before November 30, 1989, Accounting Principles Board Opinions or any Accounting Research Bulletins unless those pronouncements conflict with or contradict GASB pronouncements.

D. Use of Estimates

A number of estimates and assumptions relating to the reporting of revenues, expenditures/expenses, assets and liabilities, and the disclosure of contingent liabilities were used to prepare these financial statements in conformity with accounting principals generally accepted in the United States of America. Actual results could differ from those estimates.

E. New Pronouncements

In June 2004, GASB issued Statement No. 45, *Accounting and Financial Reporting by Employers for Post-employment Benefits Other Than Pensions*, which addresses how state and local governments should account for and report their costs and obligations related to post-employment healthcare and other non-pension benefits. Collectively, these benefits are commonly referred to as other post-employment benefits or OPEB. The statement generally requires that employers account for and report the annual cost of OPEB and the outstanding obligations and commitments related to OPEB in essentially the same manner as they currently do for pensions. Annual OPEB cost for most employers will be based on actuarially determined amounts that, if paid on an ongoing basis, generally would provide sufficient resources to pay benefits as they come due. This statement's provisions may be applied prospectively and do not require governments to fund their OPEB plans. An employer may establish its OPEB liability at zero as of the beginning of the initial year of implementation; however, the unfunded actuarial liability is required to be amortized over future periods. This statement also establishes disclosure requirements for information about the plans in which an employer participates, the funding policy followed, the actuarial valuation process and assumptions, and, for certain employers, the extent to which the plan has been funded over time. Application of this statement is effective for the City's fiscal year ended June 30, 2008. The additional disclosure concerning the implementation of GASB 45 is available in Note IV.

In May 2007, GASB issued Statement No. 50, *Pension Disclosures*, which more closely aligns the financial reporting requirements for pensions with those for other postemployment benefits (OPEB) and, in doing so, enhances information disclosed in notes to financial statements or presented as required supplementary information (RSI) by pension plans and by employers that provide pension benefits. The reporting changes required by this Statement amend applicable note disclosure and RSI requirements of Statements No. 25, *Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans,* and No. 27, *Accounting for Pensions by State and Local Governmental Employers,* to conform with requirements of Statements No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans,* and No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions.* Application of this statement is effective for the City's fiscal year ended June 30, 2008. The additional disclosure concerning the implementation of GASB 50 is available in Note IV.

The City is currently analyzing its accounting practices to determine the potential impact on the financial statements for the following Governmental Accounting Standards Board (GASB) Statements:

In November 2006, GASB issued Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations,* which addresses accounting and financial reporting standards for pollution (including contamination) remediation obligations, which are obligations to address the current or potential detrimental effects of existing pollution by participating in pollution remediation activities such as site assessments and cleanups. The scope of the statement excludes pollution prevention or control obligations with respect to current operations and future pollution remediation activities that are required upon retirement of an asset, such as landfill closure and postclosure care and nuclear power plant decommissioning. Application of this statement is effective for the City's fiscal year ending June 30, 2009.

In June 2007, GASB issued Statement No. 51, *Accounting and Financial Reporting for Intangible Assets*. This Statement requires that all intangible assets not specifically excluded by its scope provisions be classified as capital assets. Accordingly, existing authoritative guidance related to the accounting and financial reporting for capital assets should be applied to these intangible assets, as applicable. This Statement also provides authoritative guidance that specifically addresses the nature of these intangible assets. Such guidance should be applied in addition to the existing authoritative guidance for capital assets. Application of this statement is effective for the City's fiscal year ending June 30, 2010.

In June 2008, GASB issued Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*. The Statement specifically requires governments to measure and report most derivative instruments at fair value in their financial statements that are prepared using the economic resources measurement focus and the accrual basis of accounting. The requirement of reporting the derivative instruments at fair value on the face of financial statements gives the users of financial statements a clearer look into the risks their governments are sometimes exposed to when they enter into these transactions and how those risks are managed. The Statement also addresses hedge accounting requirements and improves disclosures, providing a summary of the government's derivative instrument activity, its objectives for entering into derivative instruments, and their significant terms and risks. Application of this Statement is effective for the City's fiscal year ending June 30, 2010.

F. Assets, Liabilities, and Net Assets or Equity

1. Cash and Cash Equivalents

Restricted and unrestricted pooled cash and investments held in the City Treasury and other unrestricted investments, invested by the City Treasurer, are considered cash equivalents for purposes of the statement of cash flows because the City's cash management pool and funds invested by the City Treasurer possess the characteristics of demand deposit accounts. Other restricted and unrestricted investments with maturities less than three months at the time of purchase are also considered cash equivalents for purposes of the statement of cash flows.

2. Equity in Pooled Cash and Investments Held in City Treasury

Most cash balances of the City's funds and some of its component units are pooled and invested by the City Treasurer unless otherwise dictated by legal or contractual requirements. Income and losses arising from the investment activity of pooled cash are allocated to the participating funds and component units on a monthly basis, based on their proportionate shares of the average weekly cash balance.

3. Deposits and Investments

Investments are accounted for in accordance with the provisions of GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools.*

This Statement requires governmental entities to report investments at fair value in the statement of net assets or balance sheet and to recognize the corresponding change in fair value of investments in the year in which the change occurred.

Pooled Cash and Investments held in City Treasury. The City reports its investments held in City Treasury at fair value. The fair value is based on quoted market information obtained from fiscal agents or other sources. Income from some investments is allocated directly to the General Fund rather than the fund that holds the investment on which the income was earned. The assignment of the income from these investments is supported by legal or contractual provisions approved by the City Council. For the fiscal year ended June 30, 2008, the total investment income from these funds allocated to the General Fund was approximately $4,549,000.

Retirement Systems. Investments of the Retirement Systems are reported at fair value and include securities lending transactions. Securities traded on a national or international exchange are valued at the last reported sales price on the last business day of the fiscal year at current exchange rates, if applicable. Investments that do not have an established market are reported at estimated fair value. The fair value of the private equities are based on actual cash flows to/from the Retirement Systems and the transactions and unrealized gain/loss as ascertained from the most recently available investor reports or financial statements issued by the manager of those funds. The fund manager provides an estimated unrealized gain/loss of the fund based on the financial statements and other portfolio information received from their underlying portfolio partnerships. The fair value of real estate investments is based on independent appraisals. The Retirement Systems investments in pooled holdings have the accompanying securities held by the fund manager in accordance with the above standards. At June 30, 2008, the Retirement Systems had the following pooled holdings: $18,640,000 in fixed income, $340,066,000 in international equities, $355,892,000 in domestic equities, $164,582,000 in real estate, and $121,056,000 in private equities. Purchases and sales of securities are reflected on the date of trade. Investment income is recognized as earned. Rental income from real estate activity is recognized as earned, net of expenses.

Other Investments. Non-pooled investments are generally carried at fair value. However, investments in investment agreements are carried at cost. Income from non-pooled investments is recorded based on the specific investments held by the fund. The interest income is recorded in the fund that earned the interest.

4. Inventory

Inventory of proprietary funds is valued at the lower of cost (first-in/first-out) or market. In the governmental funds, inventory items are valued at average cost. Inventories of governmental funds are recorded as expenditures when consumed rather than when purchased.

5. Special Assessment Districts

Special assessments are recorded as receivables when they become a lien on property. Special assessments not considered available are recorded as receivables and offset by deferred revenues in the governmental fund financial statements. The special assessment bonds are fully secured by liens against the privately owned properties benefited by the improvements for which the bonds were issued. There is no reserve for delinquent receivables since priority liens exist against the related properties and hence the City's management believes value will ultimately be received by the City. Surplus funds remaining at the completion of a special assessment district project are disposed of in accordance with the City Council's resolutions and with the applicable assessment bond laws of the State of California. A liability is recorded for the balance remaining until a final legal determination has been made.

6. Advances and Deposits

Amounts deposited in connection with eminent domain proceedings and special assessment surpluses are reported as advances and deposits. In the governmental fund statements, non-current portions of these are offset equally by either a deferred credit or a fund-balance reserve account indicate they do not constitute expendable financial resources available for appropriation.

7. Other Assets

Other assets primarily consist of real properties acquired outright and/or through foreclosure in connection with the housing rehabilitation program. These assets are recorded at the lower of cost or estimated net realizable value.

8. Bond Issuance Costs; Original Issue Discounts and Premiums and Deferred Amounts on Refundings

In the government-wide financial statements and the proprietary fund financial statements, long-term debt and other long-term obligations are reported as liabilities in the applicable governmental activities, business-type activities, or proprietary fund statement of net assets. Bond premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the bonds. Bonds payable are reported net of the applicable bond premium or discount. Bond issuance costs are deferred and are amortized over the term of the related debt. Gains or losses occurring from advance refundings, completed subsequent to June 30, 1993, are deferred and amortized into expense for both business-type activities and proprietary funds. For governmental activities, they are deferred and amortized into expense if they occurred subsequent to June 30, 2001.

In the fund financial statements, governmental fund types recognize bond premiums and discounts, as well as bond issuance costs, during the current period. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as debt service expenditures.

9. Restricted Assets

Assets that are restricted for specific uses by bonded debt requirements, grant provisions or other requirements are classified as restricted because they are maintained in separate bank accounts or by fiscal agents and their use is limited by applicable bond covenants or agreements.

10. Capital Assets

Capital assets include land, buildings, improvements, vehicles and equipment, infrastructure and all other tangible and intangible assets that are used in operations and that have initial useful lives extending beyond a single reporting period. Capital assets are reported in the applicable governmental or business-type activity columns in the government-wide financial statements and the proprietary funds' statement of net assets. Capital assets are defined as assets with an initial individual cost of more than $5,000 for general capital assets and $100,000 for major infrastructure assets, and an estimated useful life in excess of one year. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value at the time received. Capital outlay is recorded as expenditures of the governmental funds and as assets in the government-wide financial statements to the extent the City's capitalization threshold is met. Interest incurred during the construction phase of capital assets of business-type activities is reflected in the capitalized value of the asset constructed, net of interest earned on the invested proceeds over the same period. Amortization of assets acquired under capital leases is based on the shorter of the lease term or the estimated useful life of the asset and is included in depreciation and amortization.

Buildings and improvements, infrastructure, and vehicles and equipment are depreciated using the straight-line method over the following estimated useful lives:

Buildings	5 – 40 years
Improvements, other than buildings	10 - 50 years
Infrastructure	25 - 50 years
Vehicles and equipment	2 - 40 years
Furniture and fixtures	10 years
Intangible assets	40 years

Capital assets which are used for general governmental purposes and are not available for expenditure are accounted for and reported on in the government-wide financial statements. Capital assets that meet the definition of the major infrastructure networks or extend the life of existing infrastructure networks are capitalized as infrastructure. Infrastructure networks include road, bridges, drainage systems, and lighting systems.

11. Compensated Absences – Accrued Vacation, Sick Leave, and Compensatory Time

Vacation, sick leave, compensatory time, and related benefits are accrued as determined by the agreement between the City and the employees' group. For governmental funds, compensated absence obligations are recorded in the appropriate governmental funds when due. The portion not currently due is recorded in the government-wide financial statements. For enterprise funds, compensated absences are expensed when earned by employees. At year-end, the accrued but unpaid compensated absence obligations are recorded as current and non-current liabilities in the appropriate enterprise funds.

Vacation pay may be accumulated up to two times the annual accrual rate, not to exceed a maximum of 400 hours for non-sworn employees.

Employees represented by the San Jose Police Officer's Association (SJPOA) and International Association of Firefighters (IAFF), Local 230 (on a 40-hour workweek), may carry over to the next payroll calendar year not more than 200 hours of unused vacation leave. IAFF represented employees on a 56-hour workweek may not carry over more than 240 hours of unused vacation leave.

Employees in the Federated City Employees Retirement System who retire with at least 15 years of service (20 years for police officers and firefighters in the Police & Fire Department Retirement Plan) are eligible to receive, upon retirement, sick leave payouts based on percentages of accumulated sick hours as determined by the respective Agreements.

The following table outlines payout percentages for full-time and deferred vested employees with higher levels of sick leave balances than the minimums noted above:

Employee Type	Retirement Plan	800 to 1,200 Hours (1,120 - 1,680 for Firefighters)	Greater than 1,200 Hours (1,680 for Firefighters)
Management	Federated	75%	75% up to 1,392 Hours
Non-Management	Federated	75%	No payout beyond 1,200 Hours
All Employee Types	Police and Fire	80%	100%

12. Inter-fund Transactions

Inter-fund transactions are reflected as loans, services provided, reimbursements and/or transfers. Loans and balances related to unsettled service transactions are reported as receivables and payables as appropriate, are subject to elimination upon consolidation of similar fund types, and are referred to as either "due to/from other funds" (i.e., the current portion of inter-fund loans and unsettled service transactions) or "advances to/from other funds" (i.e., the non-current portion of inter-fund loans). Any residual balances outstanding between the governmental activities and the business-type activities are reported in the government-wide financial statements as "internal balances". Advances to other funds, as reported in the fund financial statements, are offset by a fund-balance reserve account in applicable governmental funds to indicate that they are not available for appropriation and are not available financial resources.

Services provided are deemed to be at market or near market rates and are treated as revenues and expenditures/expenses. Reimbursements are defined as when one fund incurs a cost, charges the appropriate benefiting fund and reduces its related cost as a reimbursement. All other inter-fund transactions are treated as transfers. Transfers between governmental or proprietary funds are netted as part of the reconciliation to the government-wide presentation.

13. Self-Insurance

The City is self-insured for workers' compensation, general liability, auto liability, and certain other risks. The City's workers' compensation activities are funded and accounted for separately in the fund financial statements based upon the activities of each fund. The current portion of claims liability is accounted for in the General Fund and the enterprise funds on the basis of settlements reached or judgments entered within the current fiscal year. In the government-wide financial statements and the enterprise fund financial statements, the estimated liability for all self-insurance liability claims is recorded as a liability.

14. Net Assets/Fund Equity

The government-wide and proprietary fund financial statements utilize a net assets presentation. Net assets are categorized as invested in capital assets (net of related debt), restricted, and unrestricted.

- *Invested In Capital Assets, Net of Related Debt* - This category groups all capital assets, including infrastructure, into one component of net assets. Accumulated depreciation and the outstanding balances of debt that are attributable to the acquisition, construction, or improvement of these assets reduce the balance in this category.

- *Restricted Net Assets* – This category represents net assets that have external restrictions imposed by creditors, grantors, contributors or laws or regulations of other governments and restrictions imposed by law through constitutional provisions or enabling legislation. At June 30, 2008, the government-wide statement of net assets reported restricted assets of $662.9 million in governmental activities and $160.2 million in business type activities. Of these amounts $348.0 million and $68.1 million, respectively are restricted by enabling legislation.

- *Unrestricted Net Assets* – This category represents net assets of the City, not restricted for any project or other purpose.

In the governmental fund financial statements, reserves and designations segregate portions of fund balance that are either not available or have been earmarked for specific purposes. The various reserves and designations are established by actions of the City Council and management and can be increased, reduced or eliminated by similar actions.

Reservations of fund balance are described as follows:

- *Encumbrances* - to reflect the outstanding contractual obligations for which goods and services have not been received.

- *Non-current advances, loans, other assets, and cash commitments* - to reflect the portion of assets that are not currently available as a spendable resource.

- *Debt service* - to reflect the funds held by trustees or other fiscal agents for future payment of principal and interest related to bond issue. These funds are not available for general operations.

Portions of unreserved fund balance may be designated to indicate tentative plans for financial resource utilization in a future period. Such plans or intent are subject to change and have not been legally authorized or may not result in expenditures. Fund balance designations include:

- *Contingencies* - to reflect management's intent to expend certain funds for future unanticipated needs.

- *Future projects and redevelopment activities* - to reflect management's intent to expend certain funds approved for capital projects in prior years but not yet completed.

The unreserved governmental fund balance designations at June 30, 2008 are composed of the following (dollars in thousands):

	General Fund	Redevelopment Agency	Housing Activities	Special Assessment Districts	San Jose Financing Authority	Nonmajor Funds	Total
Unreserved, designated for:							
Future projects	$ 69,029	-	-	14,013	-	451,527	$ 534,569
Contingencies	63,840	-	-	-	-	-	63,840
Undesignated	95,753	82,548	14,197	-	(31,067)	-	161,431
Total unreserved fund balances	$ 228,622	82,548	14,197	14,013	(31,067)	451,527	$ 759,840

15. Property Taxes

Property taxes are collected on behalf of and remitted to the City by Santa Clara County (the County). The amount of property tax levies is restricted by Article 13A of the California State Constitution (commonly referred to as Proposition 13).

The County assesses property values, levies, bills, and collects the related property taxes as follows:

	Secured	Unsecured
Valuation/lien dates	January 1	January 1
Levy dates	October 1	July 1
Due dates (delinquent after)	50% on November 1 (December 10) 50% on February 1 (April 10)	July 1 (August 31)

The City has elected to participate in the "Teeter Plan" offered by the County whereby cities receive 100% of secured property and supplemental property taxes levied in exchange for foregoing any interest and penalties collected on the related delinquent taxes. Accordingly, property taxes levied for the fiscal year are recorded as revenue when received from the County.

General property taxes are based either on a flat 1% rate applied to the fiscal 1976 full value of the property or on 1% of the sales price of the property on sales transactions and construction that occur after the fiscal 1976 valuation. Assessed values on properties (exclusive of increases related to sales and construction) can rise at a maximum of 2% per year depending on increases in the consumer price index.

The City's net assessed valuation for the fiscal year ended June 30, 2008, was approximately $119.1 billion, an increase of approximately 9% over the previous year. The tax rate was approximately $0.188 per $100 of assessed valuation, which included the 1% basic levy and additional levies for general obligation bonds Measures "O" and "P" (2000) and Measure "O" (2002).

16. Wastewater Treatment System

The Wastewater Treatment System is an enterprise of the City and is comprised of the Water Pollution Control Plant (the Plant), including South Bay Water Recycling and the San José Sewage Collection System.

The Plant provides wastewater treatment services to the City of San José and to seven other sewage collection agencies. The Clean Water Financing Authority was established to provide financing for the capital programs of the Plant including the regional water reclamation program. The City's sewer service rates pay for the City's share of the Plant operations, maintenance, and administration and capital costs.

In 1959, the City and the City of Santa Clara entered into an agreement to jointly own and operate the Plant. Under the agreement, the City of San José serves as the administering agency and is responsible for operating and maintaining the Plant. The cities share in the capital and operating costs on a pro rata basis determined by the ratio of each city's assessed valuation to the sum of both cities' assessed valuations. Annually, these percentages are determined and applied to the capital and operating costs on an accrual basis For the fiscal year ended June 30, 2008, the City's portion of the capital and operating costs was approximately 83.8% and, based on operations through the fiscal year ended June 30, 2008, the City's interest in the net assets of the Plant was approximately 80%.

II. Stewardship, Compliance, and Accountability

A. Deficit Fund Balances

Deficit fund balances of $2,183,000, $78,000, $1,266,000 and $30,973,000 were reported in non-major capital projects Fiber Optics Development Fund, the Interim City Facilities Improvement Fund, the Civic Center Improvement Fund and the City of San José Financing Authority major debt service fund, respectively. The deficit fund balance for the Fiber Optics Development Fund will be eliminated with future transfers from the General Fund. The Interim City Facilities Improvement Fund and the Civic Center Improvement Fund deficit will be eliminated with transfers made from future commercial paper proceeds. The San José Financing Authority deficit fund balance will be eliminated with future debt service transfers from other governmental funds.

III. Detailed Notes on All Funds

A. Cash, Deposits and Investments

As of June 30, 2008, total City cash, deposits and investments, at fair value, are as follows (dollars in thousands):

	Governmental Activities	Business-type Activities	Fiduciary Funds: Pension Trust	Fiduciary Funds: Private-Purpose Trust	Fiduciary Funds: Agency	Carrying Value
Equity in pooled cash and investments	$ 819,896	297,268	-	50	1,960	$ 1,119,174
Other cash and investments	6	-	-	-	-	6
Restricted investments:						
Equity in pooled cash and investments	78,712	166,784	-	-	-	245,496
Other cash and investments	485,270	585,293	-	32	-	1,070,595
Investments of retirement plans	-	-	5,044,319	-	-	5,044,319
Total deposits and investments	$ 1,383,884	1,049,345	5,044,319	82	1,960	7,479,590
Deposits						(4,474)
Investments						7,484,064
Total deposits and investments						$ 7,479,590

Pooled Cash and Investments Held in City Treasury. The City maintains a cash and investment pool that is available for use by all funds and certain component units. Each fund's portion of this pool is displayed on the accompanying governmental fund balance sheets and proprietary fund statement of net assets as "Equity in pooled cash and investments held in City Treasury."

Other Cash and Investments. The City has other investments outside the City Treasury that are invested pursuant to various governing bond covenants, San José Municipal Code or California Government Code provisions.

Other investments consist primarily of deposits and investments with trustees related to the issuance of bonds and to certain loan programs operated by the City. These investments are made either in accordance with bond covenants, and are pledged for payment of principal, interest, and specified capital improvements or in accordance with trust and grant agreements.

Investments of Retirement Plans. The Retirement Systems' funds are invested pursuant to policy guidelines established by the respective Boards. The objective of the investment policy is to maximize the expected return of the funds at an agreed upon level of risk. The Retirement Boards have established percentage guidelines for types of investments to ensure the portfolio is diversified.

Investments in forward currency contracts of the Pension Trust Funds are recorded commitments to purchase or sell stated amounts of international currency. The Retirement Systems' net position in these contracts is recorded at fair value as short-term international currency investments. The fair value of forward currency contracts is determined by quoted currency prices from national exchanges.

Investment Risk. The investments are subject to certain types of risk, including interest rate risk, credit quality risk, concentration of credit risk, custodial credit risk and foreign currency risk. These risks are addressed separately for the investments related to governmental and business-type activities and those related to the Retirement Systems, as follows:

1. Governmental and Business-Type Activities

Interest Rate Risk. Interest rate risk is the risk that changes in market rates will adversely affect the fair market value of an investment. Generally, the longer the time of maturity of an investment, the greater the sensitivity of its fair value to changes in market interest rates. Additionally, the fair values of the investments may be highly sensitive to interest rate fluctuations. One of the ways that the City manages its exposure to interest rate risk is by purchasing a combination of shorter-term and longer-term investments and by timing the cash flows from the maturities so that a portion is maturing or coming close to maturing evenly over time, as necessary to provide the cash flow and liquidity needs for operations.

The City has the ability and generally has the intention to hold all investments until their respective maturity dates. The average maturity of the City's pooled cash and investments as of June 30, 2008, was approximately 212 days. The Investment Policy does not prohibit the sale of securities prior to maturity. However any portfolio restructuring requires prior conceptual approval in writing from the City Manager and the Director of Finance. Section 14.2 of the Investment Policy further defines the parameters with respect to restructuring the portfolio.

Credit Quality Risk. Credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This risk is measured by the assignment of a rating by a nationally recognized statistical rating organization.

Investment in Local Agency Investment Fund. The City is a voluntary participant in the California Local Agency Investment Fund (LAIF) that is governed by the California Government Code under the oversight of the Local Investment Advisory Board (Board). The Board consists of five members as designated by state statute. The fair value of the City's investment in the LAIF pool is reported in the accompanying financial statements at amounts based upon the City's pro-rate share of the fair value provided by LAIF, for the entire LAIF portfolio (in relation to the amortized cost of that portfolio). The balance available for withdrawal is based on the accounting records maintained by LAIF, which are recorded on an amortized cost basis, which is different from the fair value of the City's position in the LAIF pool.

As of June 30, 2008, the City's investment in LAIF was approximately $499,579,000. The total amount recorded by all public agencies in LAIF at that date was approximately $25,161,000,000. Of that amount, 85.28% was invested in non-derivative financial products and 14.72% in structured notes and asset backed securities.

Concentration of Credit Risk. The City Council adopted an investment policy (the "Policy") on April 2, 1985, as amended on June 24, 2008, related to the City's cash and investment pool, which is subject to annual review. The Policy specifically prohibits trading securities for the sole purpose of speculating or taking an unhedged position on the future direction of interest rates. Per the Policy the investments conform to Sections 53600 et seq. of the California Government Code and the applicable limitations contained within the Policy.

The following table identifies the investment types that are authorized for the City by the California Government Code and Policy, if more restrictive:

Authorized Investment Type	Maximum Maturity	Maximum Percentage or Dollar of Portfolio	Maximum Investment in One Issuer
U.S. Treasury Obligations	5 Years	None	None
U.S. Government Agency Issues	5 Years	None	None
Bankers' Acceptances	180 Days	25%	5%
Insured Time Deposits	3 Years	$10 Million	5%
Uninsured Time Deposits	18 Months	$10 Million	5%
Commercial Paper	270 Days	20%	5%
Negotiable Certificates of Deposit	180 Days	25%	5%
Repurchase Agreements	10 Days	None	None
Reverse Repurchase Agreements	30 Days	$25 Million or 20%	Only one instrument permitted at a time
Corporate Notes	3 Years	15%	5%
Local Agency California Investment Fund	None	None	None
Money Market Mutual Funds	None	15%	5%
California Municipal Bonds – Category 1	5 Years	15%	5%
California Municipal Bonds – Category 2	5 Years	5%	5%
California Municipal Bonds – Category 3	5 Years	10 %	5%
Investment Agreements (Permitted for bond proceeds)	None	None	None

Other restrictions on investments are summarized as follows:

- Purchases of United States government agency securities are limited to issues of Federal Farm Credit Banks (FFCB), the Federal Home Loan Banks (FHLB), Federal Home Loan Mortgage Corporation (FHLMC), the Federal National Mortgage Association (FNMA), and Student Loan Marketing Association (SLMA).

- The purchase of Banker Acceptances (BAs) are limited to issues by domestic U.S. or foreign banks and which must be rated by Fitch Ratings as follows: an issuer rating of "B" or better for domestic U.S., "C" or better for California banks or "A/B"" or better for foreign banks. Additionally, foreign BAs must be in U.S. dollar denominations.

- Insured and uninsured time deposits are limited to issuances from banks and savings and loans with offices located in the San Jose area and deposits shall not exceed the net worth of that depository. Additionally, concerning uninsured time deposits, depositories must have an issuer rating of "B" or better by Fitch Ratings and be collateralized in a manner prescribed by state law for depositories.

- Investments in commercial paper are limited to investments in domestic corporations with the highest ranking or with the highest letter and number rating as provided for by the three nationally recognized rating services. Issuing corporations must be organized and operating within the U.S. and have total assets in excess of $500,000,000.

- Negotiable certificates of deposit are limited to banks and savings and loans with an issuer rating of "A/B" or better by Fitch Ratings and may not exceed the net worth of issuing institution.

- Repurchase agreements are to be executed only with primary dealers of the Federal Reserve Bank of New York and financial institutions, which have entered into the City's Master Repurchase Agreement and any subsequent amendments to the Master Repurchase Agreement. Securities accepted as collateral for the repurchase agreement are limited to U.S. Treasury or U.S. Federal Government Agencies permitted under the Policy. The market value of the securities that have been accepted as collateral shall, at the time of transfer, equal at least 102 percent face value of the repurchase agreement. For other than overnight investments, the securities transferred shall be marked to market on a daily basis and maintained at a market value to at least 102 percent of purchase agreement's face value.

- Corporate notes eligible for investment must be rated "A" or better by two of the three nationally recognized rating services.

- Funds invested in Local Agency Investment Fund, a State of California managed investment pool, may be made up to the maximum dollar amount per separate legal entity in conformity with account balance limits authorized by the California State Treasurer.

- Investments in money market mutual funds are limited to those funds registered with the Securities and Exchange Commission and for which either one of the credit criteria are met: (1) obtained the highest ranking or highest letter and numerical rating provided by no less than two nationally recognized rating services or (2) retained an investment advisor registered with the SEC or exempt from the SEC registration requirements with no less than five years experience investing in securities and obligations authorized by California Government Code Section 53601 and managing money market mutual funds with assets under management in excess of $500 million. Investments by the funds are restricted to U.S. Treasury and U.S. Government Agency backed securities permitted under the Policy and be maintained at no less than $1.00 per share.

- Reverse repurchase agreements under the Policy are limited to the lesser of $25,000,000 or 20% of the portfolio value and to those occasions where unanticipated short-term cash requirements can be met more advantageously by initiating a reverse repurchase agreement than by selling a security into the secondary market prior to maturity.

- Investment agreements may be used for the investment of bond proceeds in accordance with the permitted investment provisions of the specific bond indentures and in accordance with other safeguards outlined in the Policy to reduce the risk associated with a Provider's inability to meet its contractual obligations.

- California municipal bonds under the Policy are limited to a total of no more than 20% of the portfolio value. The Policy establishes three California municipal bond categories (1 through 3): bonds issued by the City or its agencies (as defined in the Policy), by the State of California, and by other California local agencies, respectively. Eligible securities must be rated AA or better by two nationally recognized rating services. For category 3, a rating of AAA through credit enhancements is also permitted.

The Policy permits the Director of Finance to authorize investments that depart from the Policy's numerical limits if such an action is in the best interest of the City and is otherwise consistent with the Policy and applicable City, State and federal laws. Whenever a deviation from the Policy is made, it must be reported to the City Manager and the City Council within one business day. During fiscal year ended June 30, 2008, there were no deviations from or violations against the Policy.

The Policy stipulates that no more than 5% of the total portfolio can be invested in investments of a single institution other than securities issued by the U.S. Treasury, U.S. Government Agencies (as defined in the policy) and LAIF.

The following schedule indicates the interest rate risk, credit quality risk and concentration credit risk of the City's investments, as of June 30, 2008. The credit ratings listed are for Moody's Investors Services and Standard and Poor's, respectively. Certain investments, such as obligations, which are backed by the full faith and credit of the United States Government, are exempt from credit rating disclosures (dollars in thousands):

		Maturity					
Type of Investment	Credit Rating	Under 30 Days	31 - 180 Days	181 - 365 Days	1 - 5 Years	Over 5 Years	Carrying Value
Pooled investments in the City Treasury:							
Federal Farm Credit Banks *	Aaa / AAA	-	34,690	20,263	87,381	-	142,334
Federal Farm Credit Banks - Callable	Aaa / AAA	-	-	-	14,991	-	14,991
Federal Home Loan Banks *	Aaa / AAA	-	73,350	15,164	225,403	-	313,917
Federal Home Loan Banks - Callable *	Aaa / AAA	-	10,061	-	126,820	-	136,881
Federal Home Loan Banks - Discount *	P-1 / A-1+	143,154	136	-	-	-	143,290
Federal Home Loan Mortgage Corporation *	Aaa / AAA	-	43,198	9,884	70,054	-	123,136
Federal Home Loan Mortgage Corporation - Callable	Aaa / AAA	-	-	-	40,388	-	40,388
Federal National Mortgage Association	Aaa / AAA	-	15,042	5,047	-	-	20,089
Commercial paper - Discounted	P-1 / A-1+	109,351	49,851	-	-	-	159,202
Money market mutual funds	AAAm	1,090	-	-	-	-	1,090
Negotiable certificate of deposit	P-1 / A-1+	53,994	-	-	-	-	53,994
Local agency investment fund	Not Rated	-	-	225,305	-	-	225,305
Total pooled investments in the City Treasury		307,589	226,328	275,663	565,037	-	1,374,617
Other funds:							
Federal Home Loan Banks - Discount	P-1 / A-1+	-	8,112	-	-	-	8,112
Federal Home Loan Mortgage Corporation - Discount	P-1 / A-1+	-	361	-	-	-	361
Investment agreements **	Not rated	-	-	17,398	496,734	23,749	537,881
Money market mutual funds	AAAm	244,500	-	-	-	-	244,500
Local agency investment fund	Not Rated	-	-	274,274	-	-	274,274
Total other funds		244,500	8,473	291,672	496,734	23,749	1,065,128
Total citywide investments (excluding Retirement Systems)		$ 552,089	234,801	567,335	1,061,771	23,749	2,439,745
Retirement Systems:							
Total investments in Retirement Systems (See page 61 and 62							5,044,319
Total investments							$ 7,484,064

* Investments with these issuers represent more than 5% of the City's pooled investments held in the City's Treasury.

** The City invested $514,132 in Citgroup Global Markets, Inc. investment agreements which is more than 5% of the investments held outside the City's Treasury.

Custodial Credit Risk. Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, the City will not be able to recover its deposits or will not be able to recover collateral securities that are in the possession of an outside party. The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty (e.g., broker - dealer) to a transaction, the City will not be able to recover the value of its investment or collateral securities that are in the possession of another party. The California Government Code requires that a financial institution secure its deposits made by state or local governmental units by pledging securities in an undivided collateral pool held by the depository regulated under state law (unless so waived by the governmental unit). The market value of the pledged governmental securities and/or first trust deed mortgage notes held in the collateral pool must be at least 110% and 150% of the City's deposits, respectively. The collateral is held by the pledging financial institution's trust department and is considered held in the City's name.

As of June 30, 2008, the carrying amount of the City's deposits with financial institutions was in an overdraft position amount of $4,474,000 and the bank balance was $14,816,000. The difference between the carrying amount and bank balance relates to outstanding checks and wire transfers issued against the general operating account. Of the bank balance, $500,000 was covered by Federal depository insurance and $14,316,000 was collateralized.

Foreign Currency Risk. The risk that changes in exchange rates will adversely affect the fair value of an investment. As of June 30, 2008, the investments in the City's investment pool were not subject to foreign currency risk.

2. Retirement Systems

Interest Rate Risk. The fair value of fixed-maturity investments fluctuate in response to changes in market interest rates. Increases in prevailing interest rates generally translate into decreases in fair value of those instruments. The fair value of interest sensitive instruments may also be affected by the creditworthiness of the issuer, prepayment options, relative values of alternative investments, and other general market conditions. Certain fixed maturity investments have call provisions that could result in shorter maturity periods. The Retirement Systems do not have policies for managing interest rate risk although the Retirement Systems do hold certain investments that could be affected by changes in interest rates. The Retirement Systems have investments in U.S. Government National Mortgage Association (GNMA) in the amount of $37,868,000 and U.S. government agency securities in the amount of $434,084,000 backed by mortgage pass-throughs which are sensitive to interest rate changes of which one Federal Home Loan Mortgage Corporation (FHLMC) in the amount $1,214,000 is a floating rate bond tied to the one-year CMT, $6,869,000 are floating rate securities tied to the six and twelve-month LIBOR and $1,308,000 are tied to the twelve-month MTA. Therefore, if interest rates decline, the mortgages are subject to prepayments by borrowers. However the Retirement Systems' intent is to hold all fixed maturity investments until maturity, and accordingly, fixed maturity investments are classified in the following tables as if they were held to maturity. International government bonds include $2,566,000 of a floating rate bond linked to the 10 year Japanese Government Bond that is reset semi-annually. In addition, as of June 30, 2008, $52,036,000 of the collateralized mortgage obligation (CMO) are floating rate securities tied to the one to twelve-month LIBOR; $901,000 are tied to the one-year CMT; and $8,116,000 are tied to a combination of LIBOR and CMT. Also, $20,450,000 of the other asset backed securities are floating rate bonds tied to one to twelve-month LIBOR; $13,450,000 of the corporate bonds are floating rate bonds tied to the one to twelve-month LIBOR; and $910,000 of the corporate bonds are floating rate but not tied to an index.

Custodial Credit Risk. For an investment, custodial credit risk is the risk that an entity will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party if the counterparty fails. The Retirement System's custodians hold all investments of the Retirement Systems in the Retirement Systems' name except for the assets held in pooled funds that are held under custody of the investment managers' custodian bank.

Credit Quality Risk. Credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This risk is measured by nationally recognized statistical rating organizations that provide rating of debt securities quality, based on a variety of factors, such as the financial conditions of the issuers, which provide investors with some idea of the issuer's ability to meet its obligations.

The System's assets shall generally be invested in investment grade, marketable, fixed-income securities. Domestic fixed maturity investment grade shall be defined as being rated Baa/BBB or better by two of the following three rating service: Moody's Investors Service, Standard & Poor's or Fitch Rating Services. If the ratings are provided by only two agencies and the third is non-rated, the most conservative (lowest) rating will be assigned. If only one agency assigns a rating, that rating will be used. Up to 15% investment in BB or B securities will be permitted with written authorization of the System's Board. The investment managers employed to manage domestic fixed-income securities will have discretion in the day-to-day management of the funds under their control. International fixed maturity must be at least Aa3/AA-. If the corresponding ratings assigned by S&P and Moody's are not equivalent the higher rating will be used for purposes of measuring portfolio and security quality. If a security is not rated by S&P or Moody's, the equivalent rating determined by the investment manager's research department will be used. If bonds are downgraded below the minimum credit quality allowable in the guidelines at the time of purchase, the Investment Manager is permitted to hold up to 2% of the System's portfolio managed by the individual manager, using the lower of S&P, Moody's, and Fitch's rating in the event of a split-rated security.

All domestic and international bonds and notes in which the Plan's assets are invested, and which mature one year or more from the date of original issues, are required to carry a rating of "BBB" or better by two of the following three services: Standard & Poor's, Moody's Investors Service, or Fitch Rating Services. In the event that ratings are provided by only two agencies and the third is non-rated, the most conservative (lowest) rating will be assigned. If only one agency assigns a rating, that rating will be used; or, if unrated, shall be of equivalent quality in the judgment of the investment manager to a similar domestic issue. Investment managers may, with prior written authorization, invest a maximum of 20% of their fixed income portfolio in bonds or notes that are rated B or BB. If bonds are downgraded below the minimum credit quality allowable in the guidelines at the time of purchase, the Investment Manager is permitted to hold up to 2% of the Plan's portfolio managed by the individual manager, using the lower of S&P, Moody's, and Fitch's rating in the event of a split-rated security.

The Retirement Systems may hedge against the possible adverse effects of currency fluctuations on the Retirement Systems' portfolio of international fixed income obligations when it is considered appropriate. Short-term investments may consist of commercial paper rated at least A-1 or P-1, repurchase agreements, short-term U.S. securities, and other money market investments.

The credit ratings listed below are for Moody's Investors Services and/or Standard and Poor's. Certain investments, such as obligations backed by the full faith and credit of the United States Government, are exempt from credit rating disclosure.

The following schedule indicates the credit quality rate risk of the Retirement Systems' investments, by category, as of June 30, 2008. (dollars in thousands):

Ratings		Total	Percentage
Unrated Agency	$	239,961	16.10%
Exempt		80,436	5.40%
AAA		414,690	27.83%
AA		84,333	5.66%
A		148,864	9.99%
BBB		119,300	8.01%
BB		31,666	2.13%
B		30,561	2.05%
CCC & Below		1,827	0.12%
Not Rated*		338,438	22.71%
Totals	$	1,490,076	100.00%

*Includes collective short-term investment funds, derivatives, FNMA, FHMLC, GNMA Treasury backed asset mortgages and cash equivalents.

Concentration of Credit Risk. The Retirement Systems' investment policies limit the aggregate amount that can be invested in each class of investments. The limits of each policy are as follows:

	Type of Investment	Policy Limits and Descriptions
The Plan	Domestic Equity	Minimum of 29% and maximum of 39% of the fair value of the aggregate portfolio.
	International Equity	Minimum of 10% and maximum of 25% of the fair value of the aggregate portfolio.
	Emerging Market Equity	Limited to 8% of the market value of the aggregate portfolio.
	Domestic Fixed Income	Minimum of 15% and maximum of 25% of the fair value of the aggregate portfolio.
	Long Duration Fixed Income	Limited to 7% of the fair value of the aggregate portfolio.
	Private Market Equity	Limited to 8% of the fair value of the aggregate portfolio. (The board approved temporarily placing all funds allotted to the private equity asset class into the Plan's small cap asset class.)
	Real Estate	Limited to 17% of the fair value of the aggregate portfolio. Real estate investments include: - Apartment complexes located in Houston, TX and Colorado Springs, CO. - Office buildings located in Denver, CO; San Jose, CA; Anchorage, AK and near Chicago, IL. - Warehouse located near Minneapolis, MN. (The properties have leases with various terms)
The System	Domestic Equity	Minimum of 38% and maximum of 48% of the fair value of the aggregate portfolio.
	International Equity	Minimum of 10% and maximum of 20% of the fair value of the aggregate portfolio.
	Domestic Bonds	Minimum of 24% and maximum of 34% of the fair value of the aggregate portfolio.
	Global Bonds	Minimum of 4% and maximum of 10% of the fair value of the aggregate portfolio.
	Private Market Equity	Limited to 6% of the fair value of the aggregate portfolio.
	Real Estate	Minimum of 3% and maximum 9% of the fair value of the aggregate portfolio. Real estate investments include: - Warehouse located in Northern California. - Interest in six separate real estate funds managed by third parties.

The collective short-term investment fund is used for overnight investment of all excess cash in the Retirement Systems' funds. It is invested by the Retirement Systems' custodians, and held in the Retirement Systems' custodians' names. This fund consists of:

- Short-term fixed obligations of the U.S. government or any federal agency, or of other issuers that are fully guaranteed by the U.S. government or a federal agency as to repayment of principal and the payment of interest;
- Commercial paper;
- Certificates of deposit;
- Repurchase agreements with major banks and U.S. government securities dealers that are collateralized by obligations of the U.S. government or a federal agency, or obligations fully guaranteed by the U.S. government or a federal agency; and
- Fully insured bank deposits.

As of June 30, 2008, the System and the Plan held $161,801,000 and $183,524,000, respectively, of investments issued by the Federal National Mortgage Association (including non-USD) which represents 8% and 6% of its plan net assets, respectively.

Foreign Currency Risk. The risk that changes in foreign exchange rates will adversely affect the fair value of an investment. As of June 30, 2008, the Retirement Systems were subject to foreign currency risk. To mitigate this risk, individual investment managers are permitted to defensively hedge currency to mitigate the impact on currency fluctuation on the underlying asset value.

Forward International Currency Contracts. The Retirement Systems made investments in forward currency contracts, which are commitments to purchase or sell stated amounts of international currency. The Retirement Systems utilize these contracts to control exposure and facilitate the settlement of international security purchase and sale transactions. At June 30, 2008, the Retirement Systems' net position in these contracts is recorded at fair value as forward international currency contracts. The fair values of forward currency contracts are determined by quoted currency prices from national exchanges. The Retirement Systems' investments in forward currency contracts bear credit risk in that parties to the contracts may fail to perform according to the terms of the contract. As of June 30, 2008, total commitments in forward currency contracts to purchase and sell foreign currencies for the System were $6,957,000 and $6,957,000, respectively, with market values of $6,955,000 and $6,874,000, respectively. As of June 30, 2008, total commitments in forward currency contracts to purchase and sell foreign currencies for the Plan were $3,164,000 and $3,164,000 respectively, with fair values of $3,162,000 and $3,168,000, respectively. The Retirement Systems' commitments relating to forward currency contracts are settled on a net basis.

The following tables provide information related to the various investment risks that may affect the investments of the Retirement Systems (dollars in thousands):

	Maturity						
Type of Investment	**3 Months or Less**	**3 - 6 Months**	**6 Months - 1 Year**	**1 - 5 Years**	**6 - 10 Years**	**More Than 10 Years**	**Total Fair Value**
Fixed Maturity:							
Domestic:							
U.S. Treasury Securities	6,111	3,029	-	63,781	5,440	16,872	95,233
U.S. Treasury Strips	-	-	-	-	-	4,859	4,859
GNMA	17,520	-	-	-	-	20,348	37,868
FHLB	-	-	-	2,692	856	544	4,092
FHLMC	5,686	1	-	1,049	7,357	74,666	88,759
FNMA	15,796	2,326	51	5,144	18,738	303,270	345,325
Other U.S. Gov't Agency Securities	-	-	-	466	660	6,065	7,191
Asset Backed Securities	-	-	-	19,254	16,215	21,802	57,271
Collateralized Mortgage Obligations	9	-	-	1,927	2,339	167,056	171,331
Corporate Bonds	-	611	5,546	78,051	109,808	167,454	361,470
State and Local Obligations	-	-	-	-	2,791	9,828	12,619
Collective Short Term Investments	146,931	-	-	-	-	-	146,931
Pooled Domestic Bonds	-	-	-	-	9,601	-	9,601
Total domestic maturities	192,053	5,967	5,597	172,364	173,805	792,764	1,342,550
International:							
Government bonds:							
British Pound	-	-	-	-	-	1,676	1,676
Canadian Dollar	-	-	-	165	229	-	394
Colombian Peso	-	-	-	147	436	72	655
Euro Currency	-	-	6,744	2,433	10,474	8,558	28,209
Indonesian Rupiah	-	-	-	691	-	-	691
Japanese Yen	-	-	-	14,645	7,586	6,499	28,730
New Zealand Dollar	-	-	-	-	651	-	651
Polish Zloty	-	-	-	-	1,413	-	1,413
Singapore Dollar	-	-	-	3,618	-	-	3,618
Swiss Franc	-	-	-	490	-	-	490
USD Denominated	-	-	-	-	16	2,902	2,918
Total international government bonds	-	-	6,744	22,189	20,805	19,707	69,445
Corporate Bonds:							
British Pound	-	-	-	987	2,979	797	4,763
Canadian Dollar	-	-	-	-	747	62	809
Euro Currency	-	-	-	5,162	5,518	905	11,585
Indonesian Rupiah	-	-	-	554	-	-	554
Japanese Yen	-	-	-	155	3,096	-	3,251
Malaysian Ringgit	-	-	-	3,058	-	-	3,058
South Korean Won	-	-	619	728	201	-	1,548
Swiss Franc	-	-	873	-	-	-	873
USD Denominated	359	31	-	10,187	13,816	18,662	43,055
Total international corporate bonds	359	31	1,492	20,831	26,357	20,426	69,496
Pooled International Fixed Maturity	-	-	-	-	2,895	6,144	9,039
Total international fixed maturities	359	31	8,236	43,020	50,057	46,277	147,980
Derivatives	(454)	-	-	-	-	-	(454)
Total fixed maturity	191,958	5,998	13,833	215,384	223,862	839,041	1,490,076

Type of Investment	Maturity 3 Months or Less	3 - 6 Months	6 Months - 1 Year	1 - 5 Years	6 - 10 Years	More Than 10 Years	Total Fair Value
Equities:							
Domestic							1,183,283
Pooled domestic equity							355,892
Total domestic equities							1,539,175
International:							
International currency:							
Australian Dollar							17,055
Brazilian Real							18,279
British Pound							106,228
Canadian Dollar							14,544
Czech Koruna							1,495
Danish Krone							8,991
Egyptian Pound							3,198
Euro Currency							154,683
Hong Kong Dollar							12,198
Indian Rupee							5,228
Indonesian Rupiah							4,490
Japanese Yen							119,708
Malaysian Ringgit							1,958
Mexican Peso							2,340
New Zealand Dollar							1,341
Norwegian Krone							1,183
Polish Zloty							642
Singapore Dollar							9,441
South African Rand							3,674
South Korean Won							7,556
Swedish Krona							6,079
Swiss Franc							37,815
Taiwan Dollar							4,096
Turkish Lira							952
USD Denominated							109,501
Total international currency							652,674
Pooled International Equities							340,066
Total international equities							992,740
Total equities							2,531,915
Private equity							121,056
Real Estate							329,981
Forward international currency contracts							75
Securities Lending Collateral							571,216
Total investments of retirement plans							$ 5,044,319

Securities Lending. The municipal code and the investment policies, adopted by the Boards of the Retirement Systems, permit the use of a securities lending program with its principal custodian banks (Custodians). The Retirement Systems do not have a threshold for securities lending. The investment policy of the System requires that loan maturities cannot stretch beyond one year, and no more than 15% of the portfolio can be lent longer than six months. The custodial agreements with the Retirement Systems' custodians authorize such custodian to loan securities in the Retirement Systems' investment portfolio under such terms and conditions, as the custodians deem advisable and to permit the loaned securities to be transferred into the name of the borrowers. The Retirement Systems receive a fee from the borrower for the use of the loaned securities. If the loaned securities are not returned by the borrower, the custodians are responsible for replacement of the loaned securities with other securities of the same issuer, class and denomination, or if such securities are not available on the open market, the custodians are required to credit the Retirement Systems' account with the market value of such unreturned loaned securities. All securities loan agreements can be terminated on demand within a period specified in each agreement by either the Retirement Systems or borrowers.

Securities lending collateral represents investments in an investment pool purchased with cash collateral, as well as securities collateral that may be pledged or sold without a default by the borrower. Securities lending transactions collateralized with securities that cannot be pledged or sold without borrower default are not reported as assets and liabilities in the fiduciary statement of net assets. The Retirement Systems do not match the maturities of investments made with cash collateral with the securities on loan.

The Plan authorized State Street Bank and Trust to invest and reinvest cash collateral in State Street's pooled investment vehicle which must have an effective duration of 120 days or less. Securities with maturities of 13 months or more must have a rating of A or better by at least two nationally recognized statistical rating organizations, or if unrated, be of comparable quality. Securities with maturities of less than 13 months are rated at least A-1/P-1. As of June 30, 2008, the size of the cash collateral pooled vehicle was $86.2 billion and the weighted average maturity of 41.84 days. The cash collateral investments included asset backed securities (48.91% of the pool), certificates of deposit (21.00%), corporate securities (6.15%), bank notes (14.76%), and other securities (9.18%). All of the underlying investments of the Plan's securities lending cash collateral are held by the counterparty, not in the name of the Plan.

The System authorized The Northern Trust Company to invest and reinvest cash collateral in Northern Trust's pooled investment vehicle which must have weighted average life of 60 days or less. Securities with maturities of 13 months or more must have a rating of A or better. Securities with maturities of less than 13 months are rated at least P-3. As of June 30, 2008, the size of the cash collateral pooled vehicle was $75.36 billion and the weighted average life of 36 days. The cash collateral investments included time deposits (10% of the pool), repurchase agreements (26%), asset backed securities (19%), certificates of deposit (17%), variable rate securities (14%), commercial paper (12%) and other bank notes (2%). All of the underlying investments of the System's securities lending cash collateral are held by the counterparty, not in the name of the System.

The loaned securities as of June 30, 2008 consisted of U.S. Treasury securities, U.S. government agency securities, domestic corporate bonds, international corporate bonds, international government bonds, domestic equity securities, and international equity securities. In return, the Retirement Systems receive collateral in the form of cash or securities equal to at least 102% for domestic and 105% for international of the transferred securities plus accrued interest for reinvestment.

As of June 30, 2008, the underlying securities loaned by the Retirement Systems as a whole amounted to approximately $570,927,000. The cash collateral and the non-cash collateral totaled $571,216,000 and $17,672,000, respectively. The Retirement Systems had no exposure to credit risk related to the securities lending transactions as of June 30, 2008.

The following table provides information concerning securities lent and collateral received as of June 30, 2008 (dollars in thousands):

	The Plan	The System	Total Fair Value
Type of Investment Lent			
For Cash Collateral:			
U.S. treasury notes and bonds	$ 63,449	19,883	$ 83,332
U.S. government agency securities	4,589	2,249	6,838
Domestic corporate bonds	23,931	21,933	45,864
International government bonds	-	7,524	7,524
International corporate bonds	-	1,626	1,626
Domestic equity securities	261,815	101,546	363,361
International equity securities	31,712	13,543	45,255
Total Lent for Cash Collateral	385,496	168,304	553,800
For Non-Cash Collateral:			
U.S. treasury notes and bonds	6,957	-	6,957
Domestic equity securities	5,529	3,054	8,583
International equity securities	864	723	1,587
Total Lent for Non-Cash Collateral	13,350	3,777	17,127
Total Securities Lent	$ 398,846	172,081	$ 570,927
Type of Collateral Received			
Cash Collateral	$ 397,773	$ 173,443	$ 571,216
Non-Cash Collateral:			
For lent U.S. treasury notes and bonds	7,088	-	7,088
For lent domestic equity securites	5,769	3,147	8,916
For lent international equity securities	904	764	1,668
Total Non-Cash Collateral	13,761	3,911	17,672
Total Collateral Received	$ 411,534	177,354	$ 588,888

In relation to the Plan, as of June 30, 2008, the fair value of the domestic collateral provided was 102.9%, thus meeting the Plan's policy of 102%. In addition the fair value of the international investment lent was 104.6%, thus did not meet the Plan's policy of 105% due to the daily market fluctuation. However, on July 1, 2008, borrowers delivered collateral to 105% of the fair value of international investment lent

In relation to the System, as of June 30, 2008, the fair value of the collateral provided was 103.1%, thus meeting the System's policy of 102%.

B. Receivables, Net of Allowances

Receivables at year-end of the City's major individual funds and non-major funds taken in aggregate, including the applicable allowances for uncollectible accounts are as follows (dollars in thousands):

Receivables – Governmental Activities:	General Fund	Redevelopment Agency	Housing Activities	Special Assessment Districts	Total Nonmajor Funds	Internal Service Fund	Governmental Activities
Taxes	$ 30,970	40	-	-	9,258	-	$ 40,268
Accrued interest	4,948	270	1,671	220	3,598	34	10,741
Grants	4,826	222	1,536	-	9,982	-	16,566
Special assessments	-	-	-	68,020	-	-	68,020
Other	25,406	148	7,038	-	18,712	-	51,304
Less: allowance for uncollectibles	(8,321)	(12)	-	(5)	(1,956)	-	(10,294)
Total receivables, net	$ 57,829	668	10,245	68,235	39,594	34	$ 176,605

Business-Type Activities:	Norman Y. Mineta San José International Airport	Wastewater Treatment System	Municipal Water System	Parking System	Total Business-Type Activities
Accounts	$ 9,162	3,762	3,331	67	$ 16,322
Accrued interest	4,697	1,793	114	137	6,741
Grants	2,464	970	-	-	3,434
Less: allowance for uncollectibles	(256)	(656)	(349)	(6)	(1,267)
Total receivables, net	$ 16,067	5,869	3,096	198	$ 25,230

Special assessment receivables in the amount of $68,015,000 are not expected to be collected within the subsequent year.

C. Loans Receivable

The composition of the City's loans receivable as of June 30, 2008 is as follows (dollars in thousands:

Type of Loan	General Fund	Redevelopment Agency	Housing Activities	Nonmajor Funds	Total Governmental Activities
20% Housing Program Developer, rehabilitation, second mortgage and relocation loans	$ -	-	494,374	-	$ 494,374
Loans funded by federal grants	-	-	41,434	7,845	49,279
Economic development, real estate developer and other loans	2,141	50,496	28,368	1,033	82,038
Less: allowance	-	(8,273)	(295,918)	(2,115)	(306,306)
Total loans, net	$ 2,141	42,223	268,258	6,763	$ 319,385

California Community Redevelopment Law requires that at least 20% of the incremental tax revenues generated from redevelopment project areas be used to increase, improve, and preserve the affordable housing stock for families and individuals with very low, low, and moderate incomes. In response to this requirement, the City established its 20% Housing Program to offer financial assistance to qualified developers, families, and individuals by providing loans at "below market" rates.

Typical loans and related terms are summarized as follows:

Loan Type	Interest Rate	Due
New construction and permanent	0 - 4%	up to 55 years
Multi-unit rental rehabilitation	3%	5 or more years
Take-out (first time homeowners)	4%	7 to 40 years
Home improvement	3 - 6%	1 to 30 years

Loans are secured by first, second, third or lower in lien-property deeds of trust except for take-out loans, which are all secured by second deeds of trust. Interest and principal are typically due in installments, except for take-out loans, which do not require payments until their maturity dates.

The City has also invested in multi-family rental housing projects serving low to moderate income individuals through subordinate loans with terms of up to 55 years. Generally, these loans are to be repaid through fixed payments or net cash flow payments from project operations and the term and potential risk of each loan varies. Because of the net cash flow feature of these subordinate loans, earnings and repayments are not as definite as with other loans receivable. There is greater risk of variability in the timing of payments and, potentially, a lower probability of eventual repayment on these subordinate loans than on other loan types.

The City maintains a valuation allowance against loans receivable comprised of an allowance for risk and an allowance for present value discount. The allowance for risk is maintained to provide for losses that can be reasonably anticipated. The allowance is based upon continuing consideration of changes in the character of the portfolio, evaluation of current economic conditions, and such other factors that, in the City's judgment, deserve recognition in estimating potential loan losses. The allowance for risk takes into consideration maturity dates, interest rates, and other relevant factors.

In accordance with City policy, loans are funded at below market rates of interest and include amortized net cash flow deferred repayment terms. This policy exists to enhance the well-being of the recipients or beneficiaries of the financial assistance, who, as described above, are very low, low, or moderate-income individuals or families, or developers of housing for such individuals or families.

Accordingly, for financial statement purposes, the City has established an allowance account against the loans receivable balance containing a present value discount. The present value discount gives recognition to the economic cost of providing loans at interest rates below market, and represents an estimate of the present value of projected net cash flows to the City from the loan portfolio. The present value discount attributable to the loans will be recognized as interest income only as such loans are repaid in full because of the deferred nature of the loan portfolio and the high level of uncertainty relating to the likelihood that cash flows will occur as projected. The difference between the individual outstanding loan balances and the calculated net present value of the loans results in the allowance for present value discount. Losses are recognized through charges to the allowance and any subsequent recoveries are added to the allowance.

For the fiscal year ended June 30, 2008, the City re-evaluated the methodology for the valuation allowance related to its loans receivable. Management has determined through policy that some of the loans that had previously been characterized as uncollectible or non-performing were in fact in fully current loans that have experienced better than originally expected performance. As a result of the change in methodology, the City recorded a decrease in expense of $29 million in the government wide statement of activities to decrease the loan loss reserve allowance for those loan portfolios that met the City's valuation allowance policy criteria.

The City's management believes the combined amount of the aforementioned risk and present value discount allowances is adequate to reflect the net realizable value of the Community Development Block Grant ("CDBG") loans, Home Investment Partnership Program ("HOME") loans, and 20% Housing Program loans receivable as of June 30, 2008.

In the normal course of operations for housing programs, the City has outstanding commitments to extend credit, which have been encumbered as of June 30, 2008. These commitments involve elements of credit and interest rate risk similar to those described above for outstanding loans receivable. As of June 30, 2008, amounts committed to extend credit under normal lending agreements totaled approximately $34,850,000.

D. Capital Assets

1. Summary Schedule

The following is a summary of capital assets activity for the fiscal year ended June 30, 2008 (dollars in thousands):

		Balance June 30, 2007	Additions	Deletions	Transfers	Balance June 30, 2008
Governmental activities:						
Capital assets, not being depreciated:						
Land	$	550,416	14,173	5,868	1,104	559,825
Construction in progress		296,914	92,331	8,019	(240,737)	140,489
Total capital assets, not being depreciated		847,330	106,504	13,887	(239,633)	700,314
Capital assets, being depreciated:						
Buildings		1,056,014	43,014	-	162,777	1,261,805
Improvements, other than buildings		46,788	8,123	-	71,760	126,671
Infrastructure		11,237,282	36,895	859	5,096	11,278,414
Vehicles and equipment		100,360	8,810	657	-	108,513
Furnitures & fixtures		26,382	125	-	-	26,507
Property under capital leases		13,379	-	-	-	13,379
Total capital assets, being depreciated		12,480,205	96,967	1,516	239,633	12,815,289
Less accumulated depreciation for:						
Buildings		233,874	30,812	-	-	264,686
Improvements, other than buildings		13,231	2,466	10,334	-	5,363
Infrastructure		5,025,693	303,732	402	-	5,329,023
Vehicles and equipment		84,653	5,735	654	-	89,734
Furnitures & fixtures		5,276	2,646	-	-	7,922
Property under capital leases		11,888	224	-	-	12,112
Total accumulated depreciation		5,374,615	345,615	11,390	-	5,708,840
Total capital assets, being depreciated, net		7,105,590	(248,648)	(9,874)	239,633	7,106,449
Governmental activities capital assets, net	$	7,952,920	(142,144)	4,013	-	7,806,763
Business-type Activities:						
Capital assets, not being depreciated:						
Land	$	134,926	-	-	-	134,926
Construction in progress		398,252	287,346	-	(69,410)	616,188
Total capital assets, not being depreciated		533,178	287,346	-	(69,410)	751,114
Capital assets, being depreciated:						
Buildings		504,199	400	-	68,569	573,168
Improvements, other than buildings		847,050	5,005	-	841	852,896
Vehicles and equipment		145,916	4,304	132	-	150,088
Intangible assets		15,188	-	-	-	15,188
Property under capital leases		13,406	-	-	-	13,406
Total capital assets, being depreciated		1,525,759	9,709	132	69,410	1,604,746
Less accumulated depreciation for:						
Buildings		222,865	21,662	-	-	244,527
Improvements, other than buildings		340,831	22,053	-	-	362,884
Vehicles and equipment		104,259	4,741	126	-	108,874
Intangible assets		7,256	355	-	-	7,611
Property under capital leases		9,698	455	-	-	10,153
Total accumulated depreciation		684,909	49,266	126	-	734,049
Total capital assets, being depreciated, net		840,850	(39,557)	6	69,410	870,697
Business-type activities capital assets, net	$	1,374,028	247,789	6	-	1,621,811

2. Depreciation

Depreciation expense charged to various governmental and business type activities of the City for the fiscal year ended June 30, 2008 is as follows (dollars in thousands):

Governmental activities:		
General government	$	11,468
Public safety		4,620
Capital maintenance		304,503
Community services		25,022
Sanitation		2
Total depreciation expense governmental activities	$	345,615
Business-type activities:		
Norman Y. Mineta San José International Airport	$	19,391
Wastewater Treatment System		25,256
Municipal Water System		2,592
Parking System		2,027
Total depreciation expense business-type activities	$	49,266

3. Intangible Assets

Intangible assets consist primarily of the Airport's acquisition of certain habitational rights and navigation/relocation easements made in accordance with its land acquisition program under the California Noise Reduction Act. All costs associated with such acquisitions have been capitalized as intangible assets. Amortization of such intangible assets is calculated using the straight-line method over a 40 year estimated useful life. Amortization expense that was reported for the year ended June 30, 2008 related to these acquisitions was approximately $320,000.

4. Capitalized Interest

Interest costs that related to the acquisition of buildings and improvements and equipment acquired with tax-exempt and taxable debt are capitalized for business-type activities. The amount of interest to be capitalized is calculated by offsetting interest expense incurred from the date of the borrowing until completion of the project, with interest earned on invested debt proceeds over the same period. Capitalized interest cost is prorated to completed projects based on the completion date of each project. For the year ended June 30, 2008, the total amount of interest capitalized in the Airport Enterprise Fund, net of allowable interest earned of temporary investment proceeds, was approximately $14,014,000.

5. Construction Commitments

Commitments outstanding as of June 30, 2008, related to governmental and business-type activities construction in progress totaled approximately $139,385,000 and $523,229,000 respectively.

E. Leases

The City has commitments under various operating lease agreements requiring annual rental payments, which are described as follows:

Governmental Activities

The City has ongoing commitments under operating lease agreements for business equipment, office facilities and land necessary for City operations, which expire at various dates through 2021. Each governmental fund includes the expenditures related to such lease agreements. There are both cancelable and non-cancelable lease agreements. Rental expenditures reported by the General Fund, Nonmajor Governmental Funds and the Redevelopment Agency Fund under these operating lease agreements for the fiscal year ended June 30, 2008 amounted to approximately $1,605,000, $728,000 and $3,753,000, respectively. The future minimum lease payments anticipated under the existing lease commitments, as of June 30, 2008, are as follows (dollars in thousands):

Fiscal Year Ending June 30,	General Fund	Nonmajor Governmental Funds	Redevelopment Agency	Total Govermental Activities
2009	$ 1,826	$ 768	$ 3,843	$ 6,437
2010	1,586	807	2,973	5,366
2011	883	848	2,537	4,268
2012	639	887	2,481	4,007
2013	539	688	2,122	3,349
2014-2018	-	-	2,823	2,823
2019-2021	-	-	659	659
Totals	$ 5,473	$ 3,998	$ 17,438	$ 26,909

Business-Type Activities

The Airport leases its office space under a lease agreement and a sublease. The sublease, which is for a portion of the Airport office space, expires in January 2009 and the lease agreement, as amended, for the remainder of the Airport office space expire in December 2009. Rental expense for the Airport's office space was approximately $3,107,000 for the year ended June 30, 2008. In June 2001, the Airport entered into an operating lease and maintenance agreement of 20 compressed natural gas powered buses. The term of the agreement is from March 1, 2003 to February 28, 2010. In December 2007, the Airport entered into an additional operating lease and maintenance agreement of 14 compressed natural gas powered buses. The term of the agreement is from August 1, 2008 to July 31, 2015. Rental expenses for the Airport buses for the year ended June 30, 2008 was approximately $2,058,000.

The future minimum payments anticipated under these commitments, as of June 30, 2008, are as follows (dollars in thousands):

Fiscal Year Ending June 30,	Operating Leases
2009	$ 5,833
2010	4,023
2011	1,354
2012	1,393
2013	1,434
2014 - 2016	3,263
Total	$ 17,300

The City also leases building space, facilities, and/or the privilege of operating a concession to tenants and concessionaries resulting in receipt of annual rents, which are described as follows:

Governmental Activities

In October 1991, the City entered into a 15-year agreement (the initial term) with the San José Arena Management Corporation (the Manager), an unrelated entity, regarding the management, operations, and maintenance of the San José Arena, and use of the San José Arena by the San José Sharks, a franchise of the National Hockey League. The agreement was subsequently amended on December 9, 2000 extending the agreement for an additional 10 years (the extended term). The initial term commenced on October 24, 1991 and terminates on July 31, 2008. The extended term commences on August 1, 2008 and terminates on July 31, 2018. Under the initial term of the agreement, the Manager is required to pay the City an annual payment amounting to the greater of $1,000,000 or 5% of the Average Annual Hockey Revenue, as defined by the agreement. Additionally, the City received a portion of the luxury-box suite revenue. During the extended term of the agreement, the Manager is required to pay the City annual, minimum rental and hockey rental payments of $1,642,000 and $1,460,000, respectively, as defined by the agreement. The fiscal year ended June 30, 2008 was year 15 of the lease for which the City received approximately $2,702,000. As of June 30, 2008, leased assets had total historic cost of approximately $117,445,000 and accumulated depreciation of approximately $38,674,000.

Business-Type Activities

The City entered into a new airline lease agreement, which took effect on December 1, 2007 and is scheduled to expire on June 30, 2012. It may be extended for one additional five-year term by mutual agreement of the City and the Signatory Airlines. The key provisions in the new airline lease agreement include compensatory rate making for the terminal cost center and residual rate making for the airfield cost center. The new airline lease agreement also includes a revenue sharing provision to evenly divide net unobligated Airport revenues between the Airport and the airlines currently operating at the Airport after each fiscal year. In any fiscal year in which there are net unobligated Airport revenues and all requirements of the City's Airport financing documents have been satisfied, the remaining net unobligated Airport revenues are to be evenly divided between the City and the airlines. If net revenues exceed the projected levels outlined in the Airport Forecast identified in the new airline lease agreement, then the airlines share of the difference will be deposited into the Rate Stabilization Fund up to a cap of $9 million. Once the Rate Stabilization Fund has been fully funded or in the event that the actual net revenues do not exceed the projected net revenues, the airlines share of net revenues shall be applied as a credit to the airline terminal revenue requirement for the following fiscal year, thus reducing terminal rental rates for the following fiscal year. The first $1 million of City's share of any net revenues shall be retained by the Airport in a discretionary fund to be used for any lawful Airport purpose. The remaining balance of City's share shall be applied to the capital costs of the Airport's Master Plan Program.

For the fiscal year ended June 30, 2008, the Airport's actual revenues exceeded its expenses and reserve requirements by approximately $37,116,000. The surplus received during the fiscal year ended June 30, 2008 will be distributed in accordance of the revenue sharing provisions of the new airline lease agreement. The Airport also enters into leases with concessionaires, airline carriers, and other business entities for building space and/or the privilege of operating a concession at the Airport. The terms of these operating leases range from 1 month to 34 years. The leases with concessionaires are generally based on the greater of a percentage of their sales or a minimum annual guaranteed amount.

The future minimum rentals to be received from the aforementioned operating leases, as of June 30, 2008, are as follows (dollars in thousands):

Fiscal Year Ending June 30,		Amount
2009	$	60,260
2010		72,219
2011		64,295
2012		70,576
2013		2,551
2014-2018		19,455
2019-2023		12,757
2024-2028		12,757
2029-2033		9,978
2034-2038		8,169
2039-2043		371
Total	$	333,388

These future minimum rentals are based upon annual rates and charges agreed to by the airlines and other tenants. In addition to the future minimum rentals disclosed above, the Airport expects to receive approximately $1,191,000 from month-to-month rentals in fiscal year ending June 30, 2009. As of June 30, 2008, leased assets had historic costs of approximately $94,235,000 and accumulated depreciation of approximately $42,614,000.

F. Long-Term Debt and Other Obligations

1. Summary Schedule of Long-Term Debt

The following is a summary of long-term debt of the City as of June 30, 2008 (dollars in thousands):

	Purpose	Issue Amount	Issue Date	Final Maturity	Range of Interest Rates	Principal Payments (millions)	Balance, June 30, 2008
Governmental Activities:							
City of San Jose:							
General Obligation Bonds:							
Series 2001 (Libraries and Parks)	Community Facilities	$ 71,000	06/06/2001	09/01/2031	4.50-5.125%	2.37	$ 56,780
Series 2002 (Libraries, Parks, Public Safety)	Community Facilities	116,090	07/18/2002	09/01/2032	4.00-5.00%	3.87	96,740
Series 2004 (Libraries, Parks, Public Safety)	Community Facilities	118,700	07/14/2004	09/01/2034	4.00-5.00%	3.96	106,835
Series 2005 (Libraries and Public Safety)	Community Facilities	46,300	06/23/2005	09/01/2035	3.00-7.50%	1.54-1.55	43,220
Series 2006 (Libraries and Parks)	Community Facilities	105,400	06/29/2006	09/01/2036	4.00-5.00%	3.51-3.52	101,890
Series 2007 (Parks and Public Safety)	Community Facilities	90,000	06/20/2007	09/01/2037	4.00-8.00%	3.00	90,000
Series 2008 (Libraries and Parks)	Community Facilities	33,100	06/25/2008	09/01/2038	4.00-5.00%	0.00-1.11	33,100
							528,565
HUD Section 108 Note	Economic Development	25,810	02/10/2005	08/01/2024	Variable	0.95-2.22	24,876
City of San Jose Financing Authority:							
Lease Revenue Bonds:							
Series 1993B (Community Facilities)	Community Facilities	18,045	04/13/1993	11/15/2012	5.85-6.00%	0.25-0.33	3,534
Series 1997B (Fire, Childcare, Library Land)	Community Facilities	9,805	07/29/1997	08/01/2012	4.65-4.875%	0.37-0.41	1,935
Series 2000C (Taxable) (Ice Centre)	Refunding	22,200	12/13/2000	12/01/2021	Variable	0.98-2.05	18,900
Series 2001E (Communication Center)	Refunding	18,610	03/29/2001	05/01/2010	4.00-5.00%	2.10-4.04	6,135
Series 2002B (Civic Center Project)	Civic Center	292,425	11/14/2002	06/01/2037	3.50-5.25%	0.16-33.45	292,145
Series 2002C (Civic Center Project)	Civic Center	60,000	11/14/2002	06/01/2039	Variable	0.00-21.79	60,000
Series 2003A (Central Service Yard)	Refunding	22,625	09/18/2003	10/15/2023	3.10-4.70%	0.91-1.61	19,310
Series 2004A (Taxable) (Ice Centre)	Ice Centre	9,225	06/03/2004	12/01/2024	Variable	0.00-2.55	9,225
Series 2006A (Civic Center Project)	Refunding	57,440	06/01/2006	06/01/2039	4.00-5.00%	0.00-17.44	57,440
Series 2007A (Recreational Facilities)	Refunding	36,555	06/28/2007	08/15/2030	4.125-4.75%	0.86-2.22	35,200
Series 2008C (Hayes Mansion)	Refunding	10,915	06/26/2008	06/01/2027	Variable	0.00-4.57	10,915
Series 2008D (Taxable) (Hayes Mansion)	Refunding	47,390	06/26/2008	06/01/2025	Variable	1.01-4.20	47,390
Series 2008F (Taxable) (Land Acquisition)	Refunding	67,195	06/11/2008	06/01/2034	Variable	0.00-4.81	67,195
							629,324
Special Assessment Bonds with Limited Governmental Commitment:							
Special Assessment Bonds:							
Series 24K (Seismic Retrofit)	Seismic Retrofit	823	06/29/1993	09/02/2013	8.50%	0.01	41
Series 24Q (Hellyer-Piercy)	Public Infrastructure	27,595	06/26/2001	09/02/2023	4.80-5.875%	0.93-2.05	22,455
Series 24R (2002 Consolidated Refunding)	Consolidated Refunding	13,940	07/03/2002	09/02/2015	3.20-4.375%	1.01-1.21	8,820
Special Tax Bonds:							
CFD No. 1 (Capitol Expressway Auto Mall)	Public Infrastructure	4,100	11/18/1997	11/01/2022	5.20-5.70%	0.14-0.30	3,105
CFD No. 6 (Great Oaks-Route 85)	Public Infrastructure	12,200	12/18/2001	09/01/2023	4.50-6.00%	0.45-0.97	10,605
CFD No. 9 (Bailey/Highway 101)	Public Infrastructure	13,560	02/13/2003	09/01/2032	4.40-6.65%	0.24-0.95	12,340
CFD No. 10 (Hassler-Silver Creek)	Public Infrastructure	12,500	07/23/2003	09/01/2023	3.50-5.25%	0.48-0.94	10,785
							68,151

	Purpose	Issue Amount	Issue Date	Final Maturity	Range of Interest Rates	Principal Payments (millions)	Balance, June 30, 2008
Governmental Activities (continued):							
Redevelopment Agency:							
Tax Allocation Bonds:							
Series 1993 (Merged Area Refunding)	Advance Refundings	$ 692,075	12/15/1993	08/01/2015	6.00%	0.00-18.20	$ 71,970
Series 1997 (Merged Area)	Redevelopment Projects	106,000	03/27/1997	08/01/2028	5.375-5.625%	0.01-0.72	6,940
Series 1998 (Merged Area)	Redevelopment Projects	175,000	03/19/1998	08/01/2009	5.00%	0.55-1.51	2,050
Series 1999 (Merged Area)	Redevelopment Projects	240,000	01/06/1999	08/01/2019	4.75%	0.00-7.17	12,920
Series 2002 (Merged Area)	Redevelopment Projects	350,000	01/24/2002	08/01/2015	4.00-4.50%	0.00-11.29	22,565
Series 2003 (Merged Area)	Redevelopment Projects	135,000	12/22/2003	08/01/2033	4.00-5.00%	0.00-34.10	127,545
Series 2004A (Merged Area)	Refunding	281,985	05/27/2004	08/01/2019	4.229-5.25%	8.78-31.90	257,885
Series 2005A (Merged Area)	Refunding	152,950	07/25/2005	08/01/2028	3.50-5.00%	0.12-26.21	152,840
Series 2005B (Merged Area)	Refunding	67,130	07/25/2005	08/01/2015	4.917-5.00%	4.23-21.56	67,130
Series 2006A (Taxable) (Merged Area)	Redevelopment Projects	14,300	11/14/2006	08/01/2022	5.65%	1.80-6.00	13,300
Series 2006B (Merged Area)	Redevelopment Projects	67,000	11/14/2006	08/01/2035	4.50-5.00%	1.00-21.00	67,000
Series 2006C (Merged Area)	Refunding	423,430	12/15/2006	08/01/2032	3.75-5.00%	12.00-74.28	423,430
Series 2006D (Merged Area)	Refunding	277,755	12/15/2006	08/01/2023	4.00-5.00%	0.45-67.33	277,755
Series 2007A (Taxable) (Merged Area)	Redevelopment Projects	21,330	11/07/2007	08/01/2017	5.10%	1.66-2.67	21,330
Series 2007B (Merged Area)	Redevelopment Projects	191,600	11/07/2007	08/01/2036	4.25-5.00%	1.53-23.97	191,600
							1,716,260
Revenue Bonds (Subordinate):							
Series 1996A (Merged Area)	Redevelopment Projects	29,500	06/27/1996	07/01/2026	Variable	0.80-2.00	26,600
Series 1996B (Merged Area)	Redevelopment Projects	29,500	06/27/1996	07/01/2026	Variable	0.80-2.00	26,600
Series 2003A (Taxable) (Merged Area)	Redevelopment Projects	45,000	08/27/2003	08/01/2028	Variable	1.20-3.10	42,800
Series 2003B (Merged Area)	Redevelopment Projects	15,000	08/27/2003	08/01/2032	Variable	0.00-3.90	15,000
							111,000
City of San Jose Financing Authority Revenue Bonds (Subordinate):							
Series 2001A (4th & San Fernando)	Parking Facility	48,675	04/10/2001	09/01/2026	3.80-5.25%	1.43-3.21	41,170
Series 2001F (Convention Center)	Refunding	186,150	07/26/2001	09/01/2022	4.00-5.00%	6.76-14.73	160,070
							201,240
HUD Section 108 Note (Masson/Dr. Eu/Security)	Redevelopment Projects	5,200	02/11/1997	08/01/2016	Variable	0.27-0.47	3,220
HUD Section 108 Note (CIM Block 3/Central Place)	Redevelopment Projects	13,000	02/08/2006	08/01/2025	Variable	0.00-1.14	13,000
HUD Section 108 Note (Story/King Retail)	Redevelopment Projects	18,000	06/30/2006	08/01/2025	Variable	0.00-1.57	18,000
							34,220
CSCDA - 2005 ERAF Loan	Redevelopment Projects	19,085	04/27/2005	08/01/2015	4.46-5.01%	1.79-2.36	14,375
CSCDA - 2006 ERAF Loan	Redevelopment Projects	14,920	05/03/2006	08/01/2016	5.41-5.67%	1.31-1.91	12,695
							27,070
Housing Set-Aside Tax Allocation Bonds:							
Series 1997E (AMT) (Merged Area)	Affordable Housing	17,045	06/23/1997	08/01/2027	5.75-5.85%	0.34-3.67	17,045
Series 2003J (Taxable) (Merged Area)	Afford. Housing/Refunding	55,265	07/10/2003	08/01/2024	2.90-5.25%	2.02-3.51	45,640
Series 2003K (Merged Area)	Afford. Housing/Refunding	13,735	07/10/2003	08/01/2029	2.50-4.40%	0.23-1.07	10,010
Series 2005A (Merged Area)	Refunding	10,445	06/30/2005	08/01/2024	3.75-5.00%	0.97-2.27	10,445
Series 2005B (Taxable) (Merged Area)	Refunding	119,275	06/30/2005	08/01/2035	4.23-5.46%	0.70-8.30	116,765
Series 2005C (AMT) (Merged Area)	Afford. Housing/Refunding	33,075	06/30/2005	08/01/2035	Variable	0.10-1.57	31,385
Series 2005D (AMT) (Merged Area)	Afford. Housing/Refunding	33,075	06/30/2005	08/01/2035	Variable	0.10-1.57	31,385
							262,675
Total Governmental Activities - Bonds, Certificates of Participation and Notes Payable							$ 3,603,381
Business-type Activities:							
Norman Y. Mineta San Jose International Airport:							
Revenue Bonds:							
Series 1998A (AMT)	Refunding	14,015	01/27/1998	03/01/2018	4.40-4.75%	0.68-1.09	8,695
Series 2001A	Runway Construction	158,455	08/14/2001	03/01/2031	3.80-5.25%	3.55-10.06	142,390
Series 2002A	Refunding	53,600	01/09/2003	03/01/2018	4.776-5.375%	0.00-9.29	53,600
Series 2002B (AMT)	Refunding	37,945	01/09/2003	03/01/2012	4.679-5.00%	2.38-6.55	21,115
Series 2004C (AMT)	Airport Facilities	75,730	06/24/2004	03/01/2026	4.625-5.25%	1.00-10.59	75,730
Series 2004D	Airport Facilities	34,270	06/24/2004	03/01/2028	5.00%	0.00-12.56	34,270
Series 2007A (AMT)	Airport Facilities	545,755	09/13/2007	03/01/2047	5.00-6.00%	0.00-73.50	545,755
Series 2007B	Airport Facilities	179,260	09/13/2007	03/01/2037	4.25-5.00%	0.00-28.80	179,260
							1,060,815
Clean Water Financing Authority:							
Revenue Bonds:							
Series 2005A	Refunding	54,020	10/05/2005	11/15/2016	3.25-5.00%	4.48-5.80	45,745
Series 2005B	Refunding	27,130	10/05/2005	11/15/2020	Variable	0.00-6.88	27,130
							72,875
State of California - Revolving Fund Loan	Wastewater Facilities	73,566	Various	05/01/2019	Various	1.77-4.36	41,952
Total Business-type Activities - Bonds and Loan Payable							$ 1,175,642
Grand Total							$ 4,779,023

2. *Debt Compliance*

There are a number of limitations and restrictions contained in the various bond indentures. The City believes it is in compliance with all significant limitations and restrictions.

3. Legal Debt Limit and Margin

The City's legal debt limit (as defined by Section 1216 of the City Charter) and debt margin as of June 30, 2008, are approximately $18,395,056,000 and $17,866,491,000, respectively. In accordance with the California Community Redevelopment Law, the Redevelopment Agency establishes its own legal debt limit, based primarily on the aggregate of all future projected tax increment revenues from existing redevelopment areas.

4. Arbitrage

The Tax Reform Act of 1986 instituted certain arbitrage restrictions with respect to the issuance of tax-exempt bonds after August 31, 1986. Arbitrage regulations deal with the investment of all tax-exempt bond proceeds at an interest yield greater than the interest yield paid to bondholders. Generally, all interest paid to bondholders can be retroactively rendered taxable if applicable rebate liabilities are not reported and paid to the Internal Revenue Service (IRS) at least every five years. During the current year, the City performed calculations to determine the rebate liabilities for the tax-exempt bond issues listed above, and the amount calculated has been recorded as a liability to the IRS. The rebate liability amount is recorded as a liability in the Governmental Activities column of the government-wide statements in the amount of $1,033,000. There was not any bond issue with a positive rebate liability due for a fifth-year payment during the current year.

5. Special Assessment Bonds with Limited City Commitment

All obligations of the City under the Special Assessment Bonds are not considered general obligations of the City, but are considered limited obligations, payable solely from the assessments and from the funds pledged therefore under the Paying Agent Agreement or Fiscal Agent Agreement. Neither the faith and credit nor the taxing power of the City, or any political subdivision thereof, is pledged to the payment of the bonds. Notwithstanding any other provision of the Paying Agent Agreement, the City is not obligated to advance available surplus funds from the City Treasury to cure any deficiency in the Redemption Fund; provided, however, the City is not prevented, in its sole discretion, from so advancing funds. As of June 30, 2008, the City has recorded approximately $68,151,000 of deferred revenue and related special assessments receivables in the Special Assessment Districts Fund. These balances consist primarily of property tax assessments to be collected in the future by the County for the City for debt service.

As of June 30, 2008, there are assessment surpluses of approximately $2,431,000 that have been declared by the City Council. These are included in advances and deposits on the accompanying statement of net assets and governmental funds balance sheet. Such surpluses will either be used to correct construction deficiencies or will be returned to the assessment-district property owners.

6. Conduit Debt

The City has issued multifamily housing revenue bonds to provide funds for secured loans to builders of multifamily housing projects. The purpose of the program is to provide needed rental housing for low to moderate-income households. To comply with Internal Revenue Service requirements in order to meet the tax-exempt status, the owner is required to set aside 20% of all units built for very low-income households. The bonds are payable solely from payments made on the related secured loans. These tax-exempt housing bonds have maturity dates that are due at various dates through January 1, 2047. As of June 30, 2008, the outstanding bond issues aggregated to approximately $572,363,000.

In August 1997, the Agency served as the conduit issuer of $10,595,000 in Multifamily Housing Revenue Bonds in order to provide funds for a mortgage loan to finance a multifamily rental housing project in the Japantown Redevelopment Project Area. The Agency has no obligation for these bonds as they are secured primarily by fully modified pass-through mortgage-backed securities guaranteed as to timely payment of principal and interest by the Government National Mortgage Association. The purpose of the bonds issue was for expanding the community's supply of low to moderate-income housing and constructing a community center and retail space. The loan is secured on a non-recourse basis, and is insured by the Federal Housing Authority pursuant to and in accordance with the provisions of Section 221(d)(4) of the National Housing Act and applicable regulations there under. At June 30, 2008, the outstanding balance was approximately $9,856,000.

In April 1998, the Agency served as the conduit issuer of $38,000,000 in Multifamily Housing Revenue Bonds in order to provide funds for a mortgage loan to finance the acquisition and construction of a multifamily residential project in the Century Center Redevelopment Project Area. The Agency has no obligation for these bonds, as they will be payable solely from, secured, to the extent, and as provided in the indenture, by a pledge of certain revenues and other amounts to be received by the Agency under the Loan Agreement. The borrower, a developer, has arranged for an initial irrevocable direct pay letter of credit to be issued in favor of the trustee. These bonds were refunded in September 2007 and as of June 30, 2008, the outstanding balance was approximately $38,000,000, payable upon maturity in September 2047.

In the opinion of the City's officials, these bonds are not payable from any revenues or assets of the City. Neither the faith and credit nor the taxing power of the City, the state, or any political subdivision thereof are pledged for the payment of the principal or interest on the bonds.

7. Summary of Changes in Long-term Obligations

The changes in long-term obligations for the year ended June 30, 2008, are as follows (dollars in thousands):

	June 30, 2007	Additional Obligations, Interest Accretion and Net Increases	Current Maturities, Retirements, and Net Decreases	June 30, 2008	Amounts Due Within One Year
Governmental Activities:					
Long-term debt payable:					
General Obligation bonds	$ 510,710	33,100	(15,245)	528,565	$ 18,245
HUD Section 108 loan	25,436	374	(934)	24,876	953
San Jose Financing Authority					
Lease revenue bonds	639,228	125,500	(137,487)	627,241	6,720
Accreted interest on capital appreciation bonds	2,323	218	(458)	2,083	480
Special Assessment bonds with limited governmental commitment	71,580	-	(3,429)	68,151	3,260
Redevelopment Agency					
Revenue bonds	322,460	-	(10,220)	312,240	10,990
HUD Section 108 notes payable	34,470	-	(250)	34,220	265
Tax allocation bonds	1,796,345	212,930	(30,340)	1,978,935	38,255
California Statewide Communities Development Authority - ERAF loan	30,020	-	(2,950)	27,070	3,090
Total long-term debt payable	3,432,572	372,122	(201,313)	3,603,381	82,258
Less deferred amounts:					
For refunding	(60,663)	(1,080)	4,158	(57,585)	(4,238)
For issuance premiums	70,690	1,645	(4,570)	67,765	4,438
For issuance discounts	(3,331)	-	154	(3,177)	(110)
Total deferred amounts	6,696	565	(258)	7,003	90
Total long-term debt payable and deferred amounts	3,439,268	372,687	(201,571)	3,610,384	82,348
Other Long-term obligations:					
Loan to City (Hayes Mansion)	1,408	-	(208)	1,200	-
Arbitrage liability	1,801	-	(768)	1,033	-
Accrued vacation, sick leave and compensatory time	89,991	41,012	(36,879)	94,124	37,000
Accrued landfill postclosure costs	9,765	-	(465)	9,300	465
Estimated liability for self-insurance	150,657	16,531	(20,850)	146,338	7,500
Net pension obligation	3,239	-	(3,239)	-	-
Net other postemployment benefits (OPEB) obligation	-	66,684		66,684	-
Total other long-term obligations	256,861	124,227	(62,409)	318,679	44,965
Governmental activities long-term obligations	$ 3,696,129	496,914	(263,980)	3,929,063	$ 127,313

	June 30, 2007	Additional Obligations and Net Increases	Current Maturities, Retirements, and Net Decreases	June 30, 2008	Amounts Due Within One Year
Business-Type Activities:					
Norman Y. Mineta San Jose International Airport:					
Revenue bonds	$ 485,545	725,015	(149,745)	1,060,815	$ 11,180
Deferred amounts:					
For refunding	(3,998)	-	726	(3,272)	(645)
For issuance premiums	5,472	477	(273)	5,676	285
For issuance discounts	(2,672)	(3,197)	36	(5,833)	(40)
Clean Water Financing Authority:					
Revenue bonds	77,185	-	(4,310)	72,875	4,480
Deferred amounts:					
For refunding	(2,418)	-	271	(2,147)	(270)
For issuance premiums	1,044	-	(111)	933	111
State of California - Revolving Fund Loan	45,585	-	(3,633)	41,952	3,699
Accrued vacation, sick leave and compensatory time	8,187	5,009	(3,801)	9,395	9,395
Estimated liability for self-insurance	8,612	1,899	(1,786)	8,725	2,023
Net other postemployment benefits (OPEB) obligation	-	10,995	-	10,995	-
Business-type long-term obligations	$ 622,542	740,198	(162,626)	1,200,114	$ 30,218

Sources of funds to meet debt service requirements are revenues derived from user fees and charges for services recorded in their respective enterprise funds.

Debt service payments are made from various sources. General Obligation bonds debt service payments are made from property taxes recorded in the Nonmajor Governmental Funds. Lease Revenue Bonds debt service payments are made from lease rental revenue from "lessee" departments in the General Fund and Nonmajor Funds. Assessment Bonds debt service payments are made from property tax assessments recorded in the Special Assessment Districts Fund. Tax Allocation Bonds and Redevelopment Agency Revenue Bonds debt service payments are made from tax increment revenue recorded in the Redevelopment Agency Fund. Other Long-Term Obligations payments are primarily made from general revenue recorded in the General Fund.

8. Annual Requirements to Maturity

The annual requirements to amortize all bonds and notes outstanding as of June 30, 2008, are as follows (dollars in thousands):

	Governmental Activities				
	City of San Jose General Obligation Bonds and HUD Loan [1]		City of San Jose Financing Authority Lease Revenue Bonds [1,2,4]		
Fiscal Year Ending June 30,	Principal	Interest	Principal	Accreted Interest	Interest
2009	$ 19,198	$ 24,766	$ 6,720	$ 480	$ 28,429
2010	20,358	24,244	9,094	501	28,310
2011	20,388	23,303	5,579	521	27,900
2012	20,424	22,455	8,405	540	27,685
2013	20,470	21,573	9,589	556	27,344
2014 - 2018	103,345	94,285	64,645	-	130,040
2019 - 2023	105,584	71,087	94,585	-	113,590
2024 - 2028	101,089	46,813	112,515	-	91,989
2029 - 2033	94,380	23,050	120,290	-	68,450
2034 - 2038	47,105	4,811	163,970	-	35,340
2039 - 2043	1,100	26	31,849	-	1,700
Total	$ 553,441	$ 356,413	$ 627,241	$ 2,598	$ 580,777

	Governmental Activities			
	Special Assessment Bonds with Limited Governmental Commitment		Redevelopment Agency Bonds and HUD Loans [1,3]	
Fiscal Year Ending June 30,	Principal	Interest	Principal	Interest
2009	$ 3,260	$ 3,555	$ 52,600	$ 106,526
2010	3,396	3,417	64,650	103,810
2011	3,521	3,266	68,960	100,732
2012	3,677	3,103	72,715	97,533
2013	3,828	2,929	76,055	94,135
2014 - 2018	18,969	11,738	429,840	412,606
2019 - 2023	20,355	6,580	524,295	303,710
2024 - 2028	6,975	2,024	514,005	180,893
2029 - 2033	4,170	729	400,420	76,959
2034 - 2038	-	-	148,925	9,974
Total	$ 68,151	$ 37,340	$ 2,352,465	$ 1,486,877

	Business-Type Activities					
	Airport		Wastewater Treatment System			
	Revenue Bonds [1,4]		Revenue Bonds [1]		Loans Payable	
Fiscal Year Ending June 30,	Principal	Interest	Principal	Interest	Principal	Interest
2009	$ 11,180	$ 54,391	$ 4,480	$ 1,986	$ 3,699	$ 765
2010	11,645	53,878	4,640	1,833	3,767	697
2011	12,120	53,356	4,790	1,679	3,835	628
2012	12,620	52,801	4,945	1,503	3,905	559
2013	13,165	52,211	5,125	1,314	3,977	487
2014 - 2018	120,105	246,148	28,910	3,363	20,997	1,322
2019 - 2023	130,860	214,274	19,985	360	1,772	32
2024 - 2028	168,995	176,927	-	-	-	-
2029 - 2033	156,185	136,267	-	-	-	-
2034 - 2038	354,630	69,674	-	-	-	-
2039 - 2043	34,000	16,951	-	-	-	-
2044 - 2048	35,310	5,451	-	-	-	-
Total	$ 1,060,815	$ 1,132,330	$ 72,875	$ 12,037	$ 41,953	$ 4,490

[1] Projected interest payments for the variable rate series of bonds are based on the following rates in effect on June 30, 2008. Lease Revenue Bonds: Series 2000C (7.07%), Series 2002C (6.00%), Series 2004A (3.98%), Series 2008C (1.30%), Series 2008D (2.75%), and Series 2008F (2.60%). Redevelopment Agency Revenue Bonds: Series 1996A (1.26%), Series 1996B (1.20%), Series 2003A (2.58%), and Series 2003B (1.35%). Redevelopment Agency Housing Set-Aside Tax Allocation Bonds: Series 2005C (1.54%) and Series 2005D (1.50%). Clean Water Financing Authority Revenue Bonds: Series 2005B (1.25%). HUD Section 108 Notes: City of San Jose and Redevelopment Agency Loans (2.88%). Each series may be set at different interest rate calculation modes, including daily, weekly, monthly, and long rates.

[2] Amount shown is accreted value payable in each period. As of June 30, 2008, $2,083,000 of value had accreted on the outstanding capital appreciation bonds, which combined with the $627,241,000 of outstanding current interest bonds totals $629,324,000 of outstanding lease revenue debt.

[3] Projected debt service payments for the City of San Jose Financing Authority Series 2001A Parking Revenue Bonds and Series 2001F Lease Revenue Bonds is included in the Redevelopment Agency category, reflecting that the Redevelopment Agency is the primary source of payment for those bonds.

[4] Does not include notional amortization of outstanding commercial paper notes.

For governmental and business-type activities, the specific year for payment of estimated liabilities for loan to the City (Hayes Mansion), arbitrage liability, accrued vacation, sick leave and compensatory time, accrued landfill postclosure costs, estimated liability for self-insurance, the net pension obligation and the net OPEB obligation are not practicable to determine.

9. New Debt Issuances and Unused Authorizations

Governmental Activities

U.S. Department of Housing and Urban Development (HUD) Section 108 Loan (Land Acquisition Project Phase II). On February 10, 2005, the City of San José received a loan commitment in the amount of $25,810,000 from HUD under the Section 108 Loan Guarantee Program for the purchase of property adjacent to the Airport. On February 16, 2005, the City made an initial draw on the loan commitment in the amount of $342,000 to place a deposit on the property and pay other costs associated with the land acquisition. On May 17, 2006, the City drew an additional $25,094,000 to complete the purchase. On November 7, 2007, the City drew the final $374,000 of the loan commitment to pay costs associated with the land acquisition.

Debt service on the HUD loan is paid from the City's General Fund. The HUD Section 108 Loan bears interest at a monthly variable rate, which on June 30, 2008, was 2.88%, and has a final maturity date of August 1, 2024.

Redevelopment Agency of the City of San José Merged Area Redevelopment Project Taxable Tax Allocation Bonds, Series 2007A-T and Tax Allocation Bonds, Series 2007B. On November 7, 2007, the San Jose Redevelopment Agency (Redevelopment Agency) issued $21,330,000 of Series 2007A-T (taxable) and $191,600,000 of Series 2007B Tax Allocation Bonds (together, the "2007AB Bonds"). The proceeds of the 2007AB Bonds will be used to finance multiple redevelopment projects within the Redevelopment Agency's Merged Area Redevelopment Project. Debt service is payable from the Redevelopment Agency's tax increment revenues.

The Series 2007A-T Bonds, which are insured by XL Capital Assurance, Inc., bear interest at a fixed rate of 5.10%, and have a maturity date of August 1, 2017. The Series 2007B Bonds, which are also insured by XL Capital Assurance Inc., bear interest at fixed rates ranging from 4.25% to 5.00%, and have a final maturity date of August 1, 2036.

City of San José Financing Authority Lease Revenue Bonds, Series 2008F (Taxable) (Land Acquisition Refunding Project). On June 11, 2008, the Authority issued $67,195,000 of Series 2008F Taxable Lease Revenue Bonds. The proceeds of the Series 2008F Bonds were used to current refund the Authority's Series 2005A (taxable) and Series 2005B (AMT) Lease Revenue Bonds (together, the "2005AB Bonds") issued to finance acquisition of and improvements to the Airport West property to be temporarily used by the Airport for aviation purposes. Debt service on the Series 2008F Bonds during the period the property is used for aviation purposes will be paid from base rental payments received by the City from the Airport.

This refunding of variable-rate bonds with another series of variable-rate bonds constitutes a restructuring of the 2005AB Bonds, which had been negatively impacted by the disruptions in the financial markets related to bond insurer downgrades by the rating agencies. The Series 2008F Bonds financing structure eliminated the bond insurance which provided credit enhancement to the 2005AB Bonds and replaced it with a direct-pay letter of credit. The Series 2005AB bonds were redeemed on June 11, 2008 and have been removed from the City's basic financial statements.

The Series 2008F Bonds, which are supported by an irrevocable direct-pay letter of credit provided by Bank of America, bear interest at a weekly variable rate, which on June 30, 2008, was 2.60%, and have a final maturity date of June 1, 2034.

City of San José General Obligation Bonds, Series 2008 (Libraries and Parks Projects). On June 25, 2008, the City issued $33,100,000 of Series 2008 general obligation bonds. The proceeds will be used to fund $5,285,000 of libraries projects and $27,815,000 of parks projects. Debt service on the Series 2008 Bonds is payable from ad valorem taxes levied upon all property subject to taxation by the City. The Series 2008 Bonds bear interest at fixed rates ranging from 4.00% to 5.00%, and have a final maturity date of September 1, 2038.

At June 30, 2008, the City has issued $580,590,000 in general obligation bonds to provide funds for the acquisition and construction of major capital facilities and parks. Of this amount, as of June 30, 2008, $528,565,000 is outstanding. Of the total amount authorized to be issued of $598,820,000, there remains an unused balance of $18,230,000.

City of San José Financing Authority Lease Revenue Bonds, Series 2008C and Series 2008D (Taxable) (Hayes Mansion Refunding Project). On June 26, 2008, the Authority issued $10,915,000 of Series 2008C and $47,390,000 of Series 2008D (taxable) Lease Revenue Bonds (together, the "2008CD Bonds"). The proceeds of the Series 2008C Bonds were used to current refund the Authority's Series 2001D Lease Revenue Bonds and the proceeds of the Series 2008D Bonds were used to current refund the Authority's Series 2001B (taxable) and Series 2001C (taxable) Lease Revenue Bonds (together with the Series 2001D Bonds, the "2001BCD Bonds"). The 2001BCD Bonds were issued to finance and refinance improvements to the Hayes Mansion

Conference Center and Edenvale Garden Park. Debt service on the 2008CD Bonds will be paid from net revenues of the Hayes Mansion Conference Center or, to the extent net revenues are insufficient, the City's General Fund.

This refunding of variable-rate bonds with another series of variable-rate bonds constitutes a restructuring of the 2001BCD Bonds, which had been negatively impacted by the disruptions in the financial markets related to bond insurer downgrades by the rating agencies. The 2008CD Bonds financing structure eliminated the bond insurance which provided credit enhancement to the 2001BCD Bonds and replaced it with a direct-pay letter of credit. The 2001BCD Bonds were redeemed on June 26, 2008, and have been removed from the City's basic financial statements.

The Series 2008C Bonds, which are supported by an irrevocable direct-pay letter of credit from The Bank of Nova Scotia and the California State Teachers' Retirement System, bear interest at a weekly variable rate, which on June 30, 2008, was 1.30%, and have a final maturity date of June 1, 2027. The Series 2008D Bonds, also supported by an irrevocable direct-pay letter of credit provided by The Bank of Nova Scotia and the California State Teachers' Retirement System, bear interest at a weekly variable rate, which on June 30, 2008, was 2.75%, and have a final maturity date of June 1, 2025.

City of San José Financing Authority Lease Revenue Commercial Paper Notes Payable. On January 13, 2004, the City Council and the City of San José Financing Authority each adopted a resolution authorizing the issuance of City of San José Financing Authority tax-exempt lease revenue commercial paper notes in an amount not to exceed $98,000,000. This commercial paper program was established as a mechanism for financing public improvements of the City including the offsite parking garage for the new Civic Center and non-construction costs for technology, furniture, equipment and relocation services for the new Civic Center. On November 9, 2005, the City Council and the Authority authorized use of the commercial paper program to finance procurement costs of the City's consolidated utility billing system.

Subsequently, on June 21, 2005, the City Council and the City of San José Financing Authority each adopted a resolution authorizing the issuance of taxable lease revenue commercial paper notes, under the same $98,000,000 not to exceed limitation as the tax-exempt notes. This subsequent authorization permits the Authority to issue taxable commercial paper notes to pay for expenses otherwise authorized under the commercial paper program, but ineligible to be paid from tax-exempt commercial paper proceeds.

On November 15, 2005, the City Council and the City of San José Financing Authority each adopted a resolution expanding the capacity of the lease revenue commercial paper program from $98,000,000 to $116,000,000 and authorizing the issuance of commercial paper notes to pay a portion of the costs of the Phase II improvements at the City's Central Service Yard and a portion of the demolition and clean-up costs at the City's Main Service Yard.

On May 22, 2007, the City Council and the City of San José Financing Authority each adopted a resolution authorizing the issuance of lease revenue commercial paper notes to pay for capital improvements at the City's HP Pavilion.

Under this program, the Authority is able to issue commercial paper notes at prevailing interest rates for periods of maturity not to exceed 270 days. The commercial paper notes are secured by a pledge of lease revenues from various City assets and additionally secured by a letter of credit provided by State Street Bank and Trust Company and the California State Teachers' Retirement System (CalSTRS).

During fiscal year 2007-08, the Authority issued $807,000 of commercial paper notes for the new City Hall and offsite parking garage, $927,000 for technology, furniture and relocation services for the new City Hall, $1,000 for municipal facility improvements, $1,222,000 for the consolidated utility billing system, $626,000 for the Central Service Yard Phase II project, and $7,763,000 for capital improvements at the City's HP Pavilion.

Also during fiscal year 2007-08, the Authority redeemed $6,291,000 for technology, furniture and relocation services for the New City Hall, $128,000 for municipal facility improvements, and $1,377,000 for the consolidated utility billing system.

On June 30, 2008, $76,066,000 of Authority tax-exempt commercial paper notes were outstanding at interest rates ranging from 1.47% to 1.50%. On June 30, 2008, $7,763,000 of Authority taxable commercial paper notes were outstanding at an interest rate of 2.47%.

The changes in commercial paper payables are as follows (dollars in thousands):

June 30, 2007	Additions	Deletions	June 30, 2008
$80,279	11,346	(7,796)	$83,829

Business-Type Activities

City of San José Airport Revenue Bonds, Series 2007A (AMT) and Series 2007B. On September 13, 2007, the City issued $545,755,000 of Series 2007A and $179,260,000 of Series 2007B Airport Revenue Bonds (together, the "2007 Bonds"). The proceeds of the 2007 Bonds will be used to pay (and to redeem commercial paper notes issued to pay) a portion of the costs of Phase I of the Airport Development Program at the Norman Y. Mineta San José International Airport. Debt service on the 2007 Bonds will be paid from general airport revenues and certain other funds. The 2007 Bonds are insured by Ambac Assurance Corporation.

The Series 2007A Bonds are subject to the Alternative Minimum Tax (AMT), bear interest at fixed rates ranging from 5.00% to 6.00%, and have a final maturity date of March 1, 2047. The Series 2007B Bonds bear interest at fixed rates ranging from 4.25% to 5.00% and have a final maturity date of March 1, 2037.

A note repayment account for the Series B Commercial Paper Notes, in the amount of $32,446,000, including interest of $40,000, was funded from the 2007 Bonds proceeds and was used to current refund a portion of the outstanding Airport Series B Commercial Paper Notes when those notes matured on December 6, 2007.

Airport Commercial Paper Notes Payable. On November 2, 1999, the City Council adopted a resolution authorizing the issuance of City of San José, San José International Airport subordinated commercial paper notes in three series (Series A -- Tax-Exempt, Series B -- Subject to the AMT, Series C -- Taxable) in an amount not to exceed $100,000,000. The commercial paper program was established to provide an interim source of financing for the initial capital projects in the Airport Master Plan until a permanent financing plan was finalized and implemented. Subsequently, on April 1, 2003, the City Council authorized use of the commercial paper program to fund costs associated with implementation of the requirements under the federal Aviation and Transportation Security Act (ATSA).

On June 20, 2006, the City Council approved an expansion of the Airport commercial paper program from $100,000,000 to $200,000,000 to ensure that funding would be available for the award of the design and construction contracts related to the rephased Airport Master Plan projects. On January 9, 2007, the City Council approved an additional expansion of the Airport commercial paper program from $200,000,000 to $450,000,000 to ensure that funding would be available for the award of the design and construction contracts related to the rephased Airport Master Plan projects. Various Airport Master Plan projects over the next several years are focused on completion of the North Concourse Projects as well as the implementation of a Terminal Area Improvement Program (the "TAIP"). Additionally, the Airport CP Program may be used to pay costs related to the Airport's lease of the former FMC property and to pay debt service costs related to the City of San José Airport Revenue Bonds, Series 2004.

On March 25, 2008, the City Council approved an expansion of the Airport commercial paper program from $450,000,000 to $600,000,000 to provide sufficient capacity to refund the City's outstanding Airport Revenue Bonds, Series 2004A and Series 2004B (the "2004AB Bonds"). This refunding of variable-rate bonds with another form of variable-rate debt constitutes a restructuring of the 2004AB Bonds, which had been negatively impacted by the disruptions in the financial markets related to auction rate securities and rating agency downgrades of bond insurers. The commercial paper notes financing structure eliminated the bond insurance which provided credit enhancement to the 2004AB Bonds and replaced it with a direct-pay letter of credit. The Series 2004AB bonds were redeemed on April 4, 2008, and have been removed from the City's basic financial statements.

Under this program, the City is able to issue commercial paper notes at prevailing interest rates for periods of maturity not to exceed 270 days in the maximum amount not to exceed $450,000,000 for Series A, B, and C notes. The portion of the commercial paper program approved by the City Council prior to March 25, 2008 is secured by a subordinate pledge of the Airport's revenues and additionally secured by letters of credit provided by JPMorgan Chase Bank, Bank of America, and Dexia Credit Local. The portion of the commercial paper program approved by the City Council on March 25, 2008 in the maximum amount not to exceed $150,000,000 for the commercial paper notes in three series; Series D-Tax Exempt, Series E-Subject to AMT and Series F-Taxable, is secured by a subordinate pledge of the Airport's revenues and additionally secured by a direct-pay letter of credit provided by Lloyds TSB Bank plc.

During fiscal year 2007-08, no Series A, D, E or F commercial paper notes were issued or outstanding. During fiscal year 2007-08, the City issued $148,225,000 of Series B commercial paper notes and $28,947,000 of Series C commercial paper notes.

On June 30, 2008, $137,867,000 of Airport Series B commercial paper notes were outstanding at interest rates ranging from 1.30% to 1.45%. On June 30, 2008, $48,323,000 of Airport Series C commercial paper notes were outstanding at an interest rate of 2.80%.

The change in commercial paper payables are as follows (dollars in thousands):

June 30, 2007	Additions	Deletions	June 30, 2008
$41,424	177,172	32,406	$186,190

10. Landfill Post-closure Costs

The City has five closed landfills for which post-closure and monitoring services may be required for approximately a 30 year period which began in fiscal year 1996, coinciding with the closure of the last landfill. An estimated liability of $9,300,000 related to the closed landfills is recorded in the government-wide financial statements as of June 30, 2008. The City's Environmental Compliance Officer performs an annual evaluation of the aforementioned liability. Actual costs may be higher due to inflation, changes in technology, or changes in regulations. The City does not own or operate any open landfills at this time.

11. Estimated Liability for Self-Insurance

The City is exposed to various risks of losses related to torts, errors and omissions, general liability, injuries to employees, unemployment claims, and employee health and dental insurance. During fiscal year 2007-08, the City maintained an all-risk property policy including boiler and machinery exposures, coverage for loss due to business interruption and flood. The City did not carry earthquake insurance as it was not reasonably available. A summary of coverage is as follows:

Coverages	Coverage per Occurance	Deductible Per Occurrence
Property	$1,000,000,000	$100,000
Business Interruption	$250,000,000	$100,000
Flood Zone A and V	$25,000,000	$500,000
Flood Zone B	$50,000,000	$100,000
All Other Flood Zones	$100,000,000	$100,000

In addition, the policy limit for property damage caused by terrorism is $5 million per occurrence and in the aggregate.

The City has an airport liability policy covering the Airport, which provides a limit of $200 million combined single limit for bodily injury and property damage with a $25 million each occurrence limit for personal injury subject to a per occurrence deductible of $100,000 and an aggregate deductible of $100,000. During the past three years, there have been not been any instances that the amount of claim settlements exceeding the insurance coverage.

Claims liabilities are reported when it is probable that a loss has occurred and the amount of the loss can be reasonably estimated. The result of the process to estimate the claims liability is not an exact amount as it depends on many complex factors, such as inflation, changes in legal doctrines, new discovered information and damage awards. Accordingly, claims are reevaluated periodically to consider the effects of inflation, recent claims settlement trends (including frequency and amount of pay-outs), economic and social factors, newly discovered information and changes in the law. The estimate of the claims liability also includes increases or decreases to previously reported unsettled claims.

With respect to the general liability accrual, the City has numerous unsettled lawsuits filed or claims asserted against it as of June 30, 2008. The City Attorney and, with respect to workers' compensation claims, the City's Risk Manager have reviewed these claims and lawsuits in order to evaluate the likelihood of an unfavorable outcome to the City and to arrive at an estimate of the amount or range of potential loss to the City. The City has included a provision for losses in its claims liability for loss contingencies that are both probable and can be reasonably estimated.

Changes in the reported liability during the past two years are as follows (dollars in thousands):

Liability as of July 1, 2006	$	182,658
Claims and changes in estimates during 2007		(6,379)
Claims payments		(17,010)
Liability as of June 30, 2007		159,269
Claims and changes in estimates during 2008		22,629
Claims payments		(26,835)
Liability as of June 30, 2008	$	155,063

(a) ***Owner Controlled Insurance Programs***

On March 31, 2004, the City acquired certain liability insurance coverage (see chart below) for major components of the "2004 Security Projects" (currently referred to as the North Concourse Project) at the Norman Y. Mineta San José International Airport (the "Airport") through an Owner Controlled Insurance Program ("OCIP"). An OCIP is a single insurance program that provides commercial general liability, excess liability and workers' compensation insurance coverage for construction jobsite risks of the project owner, general contractors and all subcontractors associated with construction at the designated project site.

	2004 Security Projects	
Coverages	Limits	Deductible Per Occurrence
General Liability	$2,000,000 per occurrence/ $4,000,000 aggregate	$250,000
Workers' Compensation	Statutory	$250,000
Employers' Liability	$2,000,000 per accident	$250,000
Excess Liability	$150,000,000	None

Due to delay in completing the North Concourse Project, the City extended the original 36-month term of the OCIP to November 1, 2008, which corresponds to the anticipated completion date of the construction project. The liability coverage is based upon payroll estimate of $34.9 million for the covered North Concourse Project. In the event that the actual payroll for the covered North Concourse Project exceeds the estimated payroll or in the event the construction period extends beyond 55 months, the City will be obligated to pay increased premiums for the North Concourse OCIP and, in addition, may be required to augment the claims loss reserve.

The terms of the North Concourse OCIP require the City to fund a claims loss reserve account with AIG, the insurance carrier, in the amount of $3.9 million. The full amount of the claims loss reserve had been deposited with AIG and was recorded as advances and deposits in the accompanying statement of net assets. The claims loss reserve account is available to AIG to pay claims within the City's deductible, subject to an aggregate maximum loss exposure within coverage limits to the City of $3.9 million. Cumulative amounts of claims paid for during the fiscal year ended June 30, 2008 was $64,000. At the end of the OCIP program period, an actuarial review is to be conducted based on the claims outstanding and a portion of the unused amount is to be returned to the City, until all claims are closed and the coverage term ends.

On March 15, 2007, the City bound additional liability insurance through another OCIP for major components of the Airport's Terminal Area Improvement Program ("TAIP OCIP"). The coverages for this program are as follows:

	Terminal Area Improvement Projects	
Coverages	Limits	Deductible Per Occurrence
General Liability	$2,000,000 per occurrence/ $4,000,000 aggregate	$250,000
Workers' Compensation	Statutory	$250,000
Employers' Liability	$1,000,000 per accident	$250,000
Excess Liability	$200,000,000	None

The liability under the TAIP OCIP is based upon an estimated payroll of $92.5 million for the covered projects and a construction period of 57 months, commencing on March 15, 2007 through December 13, 2010. In the event that the actual payroll for the covered TAIP projects exceeds the estimated $92.5 million payroll or in the event the construction period extends beyond 57 months, the City will be obligated to pay increased premiums for the TAIP OCIP and, in addition, may be required to augment the claims loss reserve fund. The terms of the TAIP OCIP require the City to fund a claims loss reserve fund with AIG in the amount of $8.9 million. The claims loss reserve fund is available to AIG to pay claims within the City's deductible subject to an aggregate maximum loss exposure within coverage limits to the City of $8.9 million. The City was able to negotiate to fund 74% of the claims loss reserve. As of June 30, 2008, an amount of $4,355,000 has been deposited with AIG and was recorded as advances and deposits in the accompanying statement of net assets. The remaining balance of $2,177,000 will be payable March 2009. Claims paid as of June 30, 2008 amounted to $214,000.

12. Net Pension Obligation

The City determined the net pension obligation at transition (July 1, 1997) amounted to $2,300,000 for the Federated Employees' Retirement System (the System) in accordance with GASB Statement No. 27, *Accounting for Pensions by State and Local Governmental Employers.* The methods and assumptions that apply for the calculation of the net pension obligation are those that are used for amortizing actuarial experience gains and losses in determining the City's contribution rates. The net pension obligation has been settled in fiscal year 2008.

13. Net Other Postemployment Benefits (OPEB) Obligation

The City implemented GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, prospectively and as such, the City did not have a net OPEB obligation at transition (i.e., July 1, 2007). The Police and Fire Department Retirement Plan (the Plan) and the Federated Employees' Retirement System (the System) calculated a net OPEB obligation in accordance with GASB Statement No. 45 as discussed in Note IV A. At June 30, 2008, the City recorded a net OPEB obligation in the amount of $77,679,000 in the government-wide financial statement.

G. Inter-fund Transactions

The composition of inter-fund balances as of June 30, 2008, with explanations of significant transactions, is as follows (dollars in thousands):

1. Due from/Due to other funds

Receivable Fund	Payable Fund	Amount	
General Fund	Redevelopment Agency	601	(1)
	Nonmajor Governmental Funds	18,564	(2)
Redevelopment Agency	General Fund	1,169	(3)
	Housing Activities	80	(4)
	Nonmajor Governmental Funds	219	(5)
Housing Activities	Redevelopment Agency	8	(6)
Nonmajor Government Funds	Redevelopment Agency	2,850	(7)
	Nonmajor Governmental Funds	20,995	(8)
Wastewater Treatment System	Nonmajor Governmental Funds	409	(9)
	Municipal Water System	1,000	(10)
Airport Fund	Nonmajor Governmental Funds	14	(11)
		$ 45,909	

(1) Represents reimbursement for services performed for the Redevelopment Agency.
(2) $5,464 represents accrual of gas tax transfer, $238 represents accrual of Construction & Conveyance tax transfer and $12,862 represents short term borrowing for working capital.
(3) Represents accrual of interest receivable of pooled cash funds.
(4) Represents debt service payments for 2005 C & D variable rate demand bond series.
(5) Represents repayment of Redevelopment Agency Selma Park funds.
(6) Represents year-end tax increment accrual.
(7) $2,700 represents accrual of Tech Museum renovations expenses and $150 represents accrual for expenses related to Fire Station #2 rebuild project.
(8) Represents short-term borrowing for working capital.
(9) $50 represents short term portion of loan for Fiber Optics Conduit project and $359 represents short term portion loan for Sewer Extension program.
(10) Represents short term portion of loan for North Coyote Valley Water Project.
(11) Represents reimburseable expenses related to the Airport West project.

2. Advances to/Advances from other funds

Receivable Fund	Payable Fund		Amount	
General Fund	San José Financing Authority	$	3,338	(1)
Redevelopment Agency	Housing Activities		580	(2)
	General Fund		250	(3)
Nonmajor Governmental Funds	Redevelopment Agency		8,112	(4)
Parking System	Redevelopment Agency		6,800	(5)
Wastewater Treatment System	Nonmajor Governmental Funds		2,154	(6)
	Municipal Water System		2,696	(7)
		$	23,930	

(1) $41 represents a loan for Seismic District bond purchase and $3,297 represents a loan to support the City-owned golf course.
(2) Represents discounted loan to the YMCA Villa Nueva Housing project.
(3) Represents executive director home loan.
(4) Represents parkland vouchers fees loans for low income housing projects and is expected to be repaid in 2010.
(5) Redevelopment Agency loan from the Parking System Fund and is expected to be repaid in 2009.
(6) Represents a long-term loan for the Fiber Optics Conduit project and is scheduled to be paid within 15 years from 1996.
(7) Represents a loan for the North Coyote Valley Water Project.

3. Transfers in/Transfers out

Transfers are indicative of funding for capital projects, lease payments or debt service and subsidies of various City operations. The following schedules summarize the City's transfer activity with explanations of significant transactions (dollars in thousands):

Between Governmental and Business-type Activities:

Transfers from	Transfers to		Amount	
General Fund	Airport Fund	$	647	(1)
San Jose Financing Authority	Parking System		29	(2)
Nonmajor Governmental Funds	Airport Fund		163	(3)
	Wastewater Treatment System		122	(4)
Parking System	General Fund		5	(5)
	Redevelopment Agency		29	(6)
	Nonmajor Governmental Funds		1,373	(7)
Municipal Water System	General Fund		1,088	(8)
	San José Financing Authority		168	(9)
	Nonmajor Governmental Funds		79	(10)
Wastewater Treatment System	General Fund		5,829	(11)
	San José Financing Authority		301	(12)
	Nonmajor Governmental Funds		1,362	(13)
Airport Fund	General Fund		110	(5)
		$	11,305	

(1) Reimbursement of overpayment of Police services costs at the Airport.
(2) Transfer for joint parking project.
(3) Reimburseable expenses for the Airport West project.
(4) Transfer to the Wastewater Treatment System to return funds from the Landscape Maintenance Reserve.
(5) Transfer for other postemployment benefits.
(6) Transfer interest earned to the Redevelopment Agency per the 4th & San Fernando parking garage bond covenant.
(7) Transfer of convention center parking receipts and debt service payment.
(8) Municipal water system payments for in-lieu taxes and rate of return on assets.
(9) Transfer for commercial paper redemption expense.
(10) Transfer for debt service payments.
(11) Wastewater treatment system payments for in-lieu taxes, rent and the City's share of the utility land settlement.
(12) Transfer for the Wastewater Treatment System share of commercial paper debt service payments.
(13) Transfer for City Hall debt service payments.

Between Funds within the Governmental Activities:

Transfers from	Transfers to		Amount	
General Fund	Redevelopment Agency	$	100	(1)
	San José Financing Authority		6,222	(2)
	Nonmajor Governmental Funds		31,386	(3)
Redevelopment Agency	General Fund		594	(4)
	Housing Activities		50,843	(5)
	San José Financing Authority		3,363	(6)
	Nonmajor Governmental Funds		10,210	(7)
Housing Activities	Redevelopment Agency		18,647	(8)
	General Fund		22	(9)
	Nonmajor Governmental Funds		903	(10)
San Jose Financing Authority	General Fund		7	(11)
	Nonmajor Governmental Funds		9,317	(12)
Nonmajor Governmental Funds	General Fund		31,537	(13)
	Redevelopment Agency		4,366	(14)
	San José Financing Authority		47,847	(15)
	Nonmajor Governmental Funds		13,499	(16)
		$	228,863	

(1) Reimburse Redevelopment Agency for share of Mariachi Festival expenditures.
(2) $326 is debt service payments for Childcare portable and Fire apparatus bonds,
$364 is for City Hall debt service payments and
$5,532 is debt service payments to San José Financing Authority for 2005 Series A and B bonds.
(3) Various debt service payments, loan repayments and operating transfers.
(4) $341 for San José Arena pass through payment and $253 is for reimbursements for services received from the Redevelopment Agency.
(5) $37,068 is for 20% increment tax transfers as required under California Community Redevelopment Law and $13,775 is for transfers related to the Series 2005 bond proceeds.
(6) $3,363 is a debt service payment for the 4th & San Fernando parking garage.
(7) $10,210 is for capital projects in the redevelopment project areas.
(8) Transfer for debt service payments.
(9) Transfer for other postemployment benefits.
(10) Transfer for City Hall debt service payments.
(11) 2001D bond project funds transferred to the General Fund.
(12) $7,580 is for San José Arena reimbursement, $1,077 is for the integrated Customer Relationship Management, Utility Billing and Partner Relationship Management Systems (CUSP) account reimbursements and $660 is for various other reimbursements.
(13) Various transfers for operations and capital projects.
(14) $900 is for Starbird Youth Center project,
$1,924 is for management of demolition and clean-up of Main Yard property
and $1,542 is for various project service memorandum (PSM) refunds.
(15) Various transfers for debt service payments.
(16) Various transfers for debt service, operations and capital projects.

IV. Other Information

A. Employee Defined Benefit Retirement Systems

1. Systems Description

The City sponsors and administers two single employer defined benefit retirement systems, the Police and Fire Department Retirement Plan (the "Plan") and the Federated City Employees' Retirement System (the "System" and collectively, "the Retirement Systems"), which together cover all full-time and certain part-time employees of the City. Each of them provides postemployment health subsidy benefits in addition to regular retirement benefits. The Retirement Systems are accounted for as separate Pension Trust Funds. The estimated payrolls for employees covered under the Plan and the System for the fiscal year ended June 30, 2008, were approximately $241,781,000 and $301,266,000, respectively. The City's total payroll for the fiscal year ended June 30, 2008, was approximately $594,575,000.

The separately issued annual reports of the Retirement Systems and the City's municipal code provide more detailed information about the Retirement Systems. Those reports may be obtained by writing to the City of San José Department of Retirement Services, 1737 North First Street, Suite 580, San José, California 95112.

The Retirement Systems provide general retirement benefits under single employer Defined Benefit Pension Plans, including pension, death, disability, as well as postemployment medical and dental benefits under the Postemployment Healthcare Plans. Benefits are based on average final compensation, years of service, and limited required cost-of-living increases. The Retirement Systems are administered by the Director of Retirement, an employee of the City, under the direction of the Retirement Systems' Boards of Administration. The contribution and benefit provisions and all other requirements are established by City ordinances.

The current membership in the Retirement Systems as of June 30, 2008, is as follows:

	The Plan	The System
Defined Benefit Pension Plans:		
Retirees and beneficiaries currently receiving benefits	1,594	2,886
Terminated vested members not yet receiving benefits	74	597
Active members	2,179	4,282
Total	3,847	7,765
Postemployment Healthcare Plans:		
Retirees and beneficiaries currently receiving benefits	1,418	2,144
Terminated vested members not yet receiving benefits	11	82
Active members	2,179	4,282
Total	3,608	6,508

The Retirement Systems are not subject to the provisions of the Employee Retirement Income Security Act of 1974.

2. Funding Policy

It is the City's policy to obtain actuarial valuations for the Retirement Systems every two years. Actuarial valuations of an ongoing plan involve estimates and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, salary increases, healthcare cost trend, and investment rate of return. Actuarially determined amounts are subject to continual revisions as actual results are compared with past expectations and new estimates are made about the future.

Projections of benefit costs for financial reporting purposes are based on the substantive plan as understood by the employer and plan members, and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and the plan members to that point.

The contributions to the Defined Benefit Pension Plan for each Retirement System for both the City and the participating employees are based upon an actuarially determined percentage of each employee's base salary sufficient to provide adequate assets to pay benefits when due. The postemployment contribution rates were based upon an actuarially determined percentage of each employee's base salary prior to the requirements of GASB Statement Numbers 43 and 45. The contributions are not sufficient to provide adequate assets to pay benefits when due in accordance with the requirements of GASB Statement Numbers 43 and 45.

Contribution rates for the City and the participating employees for fiscal year 2008 through June 28, 2008 were established in accordance with actuarially determined requirements computed through actuarial valuations dated June 30, 2005 for the Defined Benefit Pension Plan and the Postemployment Healthcare Plan. Contribution rates for the City and the participating employees for the last two days of fiscal year 2008 for the Retirement Systems were based on the rates from the actuarial valuations dated June 30, 2007. The contribution rates in effect and the amounts contributed to the Plan and the System for the fiscal year ended June 30, 2008, are as follows (dollars in thousands):

	The Plan			The System		
	City	Participants	Total	City	Participants	Total
Actuarial Rate:						
Defined Benefit Plan:						
7/01/07 - 6/28/08 (police members)	24.71%	7.89%				
7/01/07 - 6/28/08 (fire members)	21.42%	7.48%				
7/01/07 - 6/28/08				18.16%	4.26%	
6/29/08 - 6/30/08 (police members)	21.61%	8.18%				
6/29/08 - 6/30/08 (fire members)	24.12%	8.62%				
6/29/08 - 6/30/08				18.31%	4.28%	
Postemployment Healthcare Plan:						
7/01/07 - 6/28/08	4.19%	3.78%		3.82%	3.32%	
6/29/08 - 6/30/08	4.19%	3.78%		5.25%	4.65%	
Annual Pension Contribution (in thousands):						
Defined Benefit Plan	$ 56,372	$ 19,210	$ 75,582	$ 54,957	$ 13,366	$ 68,323
Postemployment Healthcare Plan	10,618	9,151	19,769	11,560	10,403	21,963
	$ 66,990	$ 28,361	$ 95,351	$ 66,517	$ 23,769	$ 90,286

For the Defined Benefit Pension Plan, according to the most recent actuarial valuation dated June 30, 2005, the City's contribution rate for the Plan increased from 21.03% to 24.71% for police members, and 21.42% for fire members. The rate remained at 7.48% for the employees for fiscal year 2008. For the System, the contribution rate remained at 18.16% for the City and 4.26% for the employees for fiscal year 2008.

For the Postemployment Healthcare Plan, according to the most recent actuarial valuation dated June 30, 2005, the contribution rate for the Plan remained at 4.19% for the City and 3.78% for the employees for fiscal year 2008. For the System, the contribution rate remained at 3.82% for the City and 3.32% for the employees for fiscal year 2008.

3. Annual Pension Cost and Net Pension Obligation

The City's annual pension cost and net pension obligation for the Plan and the System as of and for the fiscal year ended June 30, 2008, were as follows (dollars in thousands):

	The Plan	The System
Annual required contribution	$ 56,372	$ 52,019
Interest on net pension obligation	-	267
Adjustment to annual required contribution	-	(568)
Annual pension cost	56,372	51,718
Contributions made	(56,372)	(54,957)
Decrease in net pension obligation	-	(3,239)
Net pension obligation – beginning of year	-	3,239
Net pension obligation – end of year	$ -	$ -

The following is three-year trend information for the City's single-employer pension plans (dollars in thousands):

	Fiscal year ended	Annual Pension Cost (APC)	Percent APC Contributed	Net Pension Obligation
The Plan	6/30/06	$ 43,473	100%	$ -
	6/30/07	46,625	100%	-
	6/30/08	56,372	100%	-
The System	6/30/06	41,267	100%	3,233
	6/30/07	51,004	100%	3,239
	6/30/08	51,718	106%	-

4. Annual Other Postemployment Benefit (OPEB) Cost and Net OPEB Obligation

As noted in Note I, the City implemented GASB 45 in fiscal year 2008 and elected to report a zero net OPEB obligation at the beginning of the transition year. The City's annual other postemployment benefit cost and net OPEB obligation for the Plan and the System as of and for the fiscal year ended June 30, 2008, were as follows (dollars in thousands):

	The Plan	The System
Annual required contribution	$ 61,344	$ 38,513
Interest on net OPEB obligation	-	-
Adjustment to annual required contribution	-	-
Annual OPEB cost	61,344	38,513
Contributions made	(10,618)	(11,560)
Increase in net OPEB obligation	50,726	26,953
Net OPEB obligation – beginning of year	-	-
Net OPEB obligation – end of year	$ 50,726	$ 26,953

The annual OPEB cost, the percentage of annual OPEB cost contributed during the fiscal year, and the net OPEB obligation at the end of the transition year for the City's single employer healthcare plans were as follows (dollars in thousands):

	Fiscal year ended	Annual OPEB Cost	Percent Annual OPEB Cost Contributed	Net OPEB Obligation
The Plan	6/30/08	$ 61,344	17%	$ 50,726
The System	6/30/08	38,513	30%	26,953

5. Funded Status and Funding Progress for Pension Plans

As of June 30, 2007, the most recent actuarial valuation date, the Plan's defined benefit pension plan was 100% funded. The actuarial accrued liability for benefits was $2,372,386,000, and the actuarial value of assets was $2,365,790,000, resulting in an unfunded actuarial accrued liability (UAAL) of $6,596,000. The covered payroll (annual payroll of active employees covered by the plan) was $227,734,000, and the ratio of the UAAL to the covered payroll was 3%. As of the June 30, 2007 valuation date, the System's defined benefit pension plan was 83% funded. The actuarial accrued liability for benefits was $1,960,943,000 and the actuarial value of assets was $1,622,851,000, resulting in an unfunded actuarial accrued liability (UAAL) of $338,092,000. The covered payroll was $291,405,000, and the ratio of the UAAL to the covered payroll was 116%.

The Schedule of Funding Progress, presented as RSI following the Notes to Basic Financial Statements, presents multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits.

6. Funded Status and Funding Progress for Postemployment Healthcare Plans

As of June 30, 2006, the most recent actuarial valuation date, the Plan's postemployment healthcare plan was 5% funded. The actuarial accrued liability for benefits was $851,217,000, and the actuarial value of assets was $38,381,000, resulting in an unfunded actuarial accrued liability (UAAL) of $812,836,000. The covered payroll (annual payroll of active employees covered by the plan) was $218,521,000, and the ratio of the UAAL to the covered payroll was 372%. As of the June 30, 2006 valuation date, the System's postemployment healthcare plan was 12% funded. The actuarial accrued liability for benefits was $702,939,000, and the actuarial value of assets was $81,288,000, resulting in an unfunded actuarial accrued liability (UAAL) of $621,651,000. The covered payroll was $275,559,000, and the ratio of the UAAL to the covered payroll was 226%.

The Schedule of Funding Progress, presented as RSI following the Notes to Basic Financial Statements, presents information as of the end of the transition year about the actuarial value of plan assets in relation to the actuarial accrued liability for benefits.

7. Actuarial Assumptions and Methods

The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrual liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations. The more significant actuarial methods and assumptions used in the calculations of employee and employer contributions to the Retirement Systems for the pension plans for the fiscal year ended June 30, 2008 are as follows:

Method/Assumption	The Plan	The System
Valuation date	June 30, 2005	June 30, 2005
Actuarial cost method	Entry age normal cost method	Entry age normal cost method
Amortization method for actuarial accrued liabilities	Level percentage of payroll	Level percentage of payroll
Remaining amortization period	12 years, closed for unfunded pension liabilities; 16 years, closed for gains and losses between valuations	30 years, open
Actuarial asset valuation method	5 year smoothed market	5 year smoothed market
Investment rate of return	8.00% per annum	8.25% per annum
Postretirement mortality	The 1994 Male Group Annuity Mortality Table, with a four-year set back, is used for male members. The 1994 Female Group Annuity Mortality Table, with a one-year set forward, is used for female members.	The 1994 Group Annuity Mortality Table used for healthy retirees and beneficiaries. The disabled mortality table used was the 1981 Disability Mortality Table.
Active service, withdrawal, death, disability service retirement	Based upon the June 30, 2005 experience analysis	Based on current experience
Salary increases	10% for employees for the first five years of service; 7% for six and seven years of service and 4.75% in excess of seven years of service. Of the total salary increases, 3% is for inflation and 1% is real across-the-board salary increases	The rate of annual salary increase for all members with at least five years of service is equal to 4.25% plus an added merit component for those with zero to four years of service.
Cost-of-living adjustments	3.00% per year	3.00% per year

8. Actuarial Methods and Assumptions for OPEB Plans

The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrual liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations. The more significant actuarial methods and assumptions used in the calculation of the annual OPEB cost, the annual required contribution, and the funded status and funding progress for the fiscal year ended June 30, 2008 are as follows:

Method/Assumption	The Plan	The System
Valuation date	June 30, 2006	June 30, 2006
Actuarial cost method	Entry age normal cost method	Entry age normal cost method
Amortization method for actuarial accrued liabilities	Level percentage of payroll	Level percentage of payroll
Remaining amortization period	30 years as of June 30, 2006, open	30 Years as of June 30, 2006, open
Actuarial asset valuation method	5 year smoothed market	5 year smoothed market
Postretirement mortality	The 1994 Male Group Annuity Mortality Table, with a four-year set back, is used for male members. The 1994 Female Group Annuity Mortality Table, with a one year set forward, is used for female members.	The 1994 Group Annuity Mortality Table used for healthy retirees and beneficiaries. The disabled mortality table used was the 1981 Disability Mortality Table.
Discount rate*	5.3%	5.6%
Salary increases	Of the total salary increases, 3% is for inflation and 1% is real across-the-board salary increase.	The rate of projected payroll increase is 4.25%.
Healthcare cost trend rate:		
Medical	12% in 2007-2008 plan year, decreasing by 1% for each year for seven years until it reaches an ultimate rate of 5%	The valuation assumes that future medical inflation will be at a rate of 12% per annum graded down each year in 1% increments to an ultimate rate of 4%.
Dental	5%	Dental inflation is assumed to be 6% graded down to 4% over a nine year period.
Inflation rate	3.00% per year	4.00% per year

* Determined as a blended rate of the expected long-term investment returns on plan assets and on the City's investments, based on the funded level of the plan at the valuation date.

B. Defined Contribution Retirement Plan

In January 1995, the Agency Board adopted a single employer defined contribution retirement plan, the Redevelopment Agency of the City of San José Retirement Plan (the Retirement Plan), which provides pension benefits for its non-civil service employees. For eligible employees who contribute 3.5% of their annual base salary, the Agency contributes approximately 9.0%. The Agency's contributions are based on a formula taking into account employee annual base salary and length of service. The Agency's contributions for each employee (and interest allocated to the employee's account) are fully vested after three years of continuous service from the original date of employment. The Agency's contributions and interest forfeited by employees who leave employment before vesting occurs may be used to reduce the Agency's contribution requirement or to offset plan-operating expenses. The Agency contracts with an advisor to manage the Retirement Plan with all assets being held in trust by a third party custodian in the name of each of the Retirement Plan's participants. Each of the Retirement Plan's participants directs the investments of his/her separate account. The Agency's Board of Directors may authorize changes to the Retirement Plan.

The Agency's total payroll in fiscal year ended June 30, 2008 for all non-civil service employees was approximately $9,259,000. Contributions to the Retirement Plan during the year ended June 30, 2008, made by both the Agency and the participating employees, amounted to approximately $859,000 and $328,000, respectively.

C. Commitments and Contingencies

1. Norman Y. Mineta San José International Airport

Purchase Commitments. As of June 30, 2008, the Airport was obligated for purchase commitments of approximately $497,173,000, primarily for the noise attenuation, design and construction of the North Concourse building and Taxiway Y reconstruction. Additionally, the Airport has projected that it will expend or encumber approximately $742,649,000 on proposed capital projects during the next five fiscal years. It is anticipated that funding for such capital projects will be provided primarily by proceeds from passenger facility charges (PFC), federal grant monies, bond proceeds and other Airport revenues.

Fuel Storage Facility. In 1985, a fuel leak was discovered in the Airport's fuel storage facility. The Airport and a fuel supplier with a fuel storage facility adjacent to the City owned facility agreed to share the costs of a study to develop an acceptable cleanup program for the contaminated site. The cleanup program submitted to the Santa Clara Valley Water District, the responsible regulatory authority, was approved and the cleanup program commenced during the fiscal year ended June 30, 1991. The agreement between the Airport and the fuel supplier required the Airport to pay 60% of the costs and the fuel supplier to pay the balance of 40% of the costs. The fuel supplier also receives a 10% management fee for overseeing the cleanup operation. As of June 30, 2008, the Airport has accrued approximately $330,000 to reflect its share of the remaining estimated costs of the initial phase of the cleanup program. On December 22, 1998, due to minimal fuel activities, the Airport temporarily closed its facility and ceased operation at that time. Construction of a new fuel storage facility started in July 2008 and it is anticipated that it will become operational in approximately October 2009. The current facility will then be closed and site remediation activities will commence.

Acoustical Treatment Program. The Airport has an Acoustical Treatment Program (ACT) to comply with the requirements of Title 21 of the California Noise Standard. The program provides acoustical treatment to residences in the noise impact areas surrounding the Airport, at no cost to the property owners. The program is primarily funded by grants from the Federal Aviation Administration (FAA) and by PFC revenues. The Airport expended approximately $11,788,000 on noise attenuation projects during the fiscal year ended June 30, 2008 and expects to spend approximately $12,836,000 during fiscal year ending June 30, 2009.

Master Plan. The Airport Master Plan consists of a program of facility improvements designed to fully accommodate commercial aviation demand (passengers and cargo) projected for the year 2017, with development phased as demand warrants and is determined to be financially feasible. The Master Plan was originally adopted by the City of San Jose in June 1997 and approved by the Federal Aviation Administration (FAA) in December 1999. In June 2006, the City Council approved revisions to the Airport Master Plan regarding implementation of the Terminal Area Improvement Program (TAIP). The current Program consists of two phases that total $1.6 billion. Phase 1 of the Program has a total budget of approximately $1.3 billion and construction of most of the projects is scheduled to be completed near the end of 2009-2010, with some projects to be completed in 2010-2011. Construction of the Phase 2 projects is contingent upon satisfying specified activity-based triggers. Funding for Master Plan projects is from several sources, including grants, PFCs, airline rates and charges, airport revenue bonds, and subordinated commercial paper proceeds.

2. Redevelopment Agency

Tax Sharing Agreement with the County of Santa Clara. On May 22, 2001, the County of Santa Clara, City of San José and the Agency amended and restated the 1993 Tax Revenue Sharing Agreement (the new agreement). The new agreement requires the Agency to provide the County a portion of the Agency's bond proceeds in addition to the 1993 revenue sharing amounts. The money will be used by the County to undertake redevelopment projects in or of benefit to the merged area, and requires the Agency to transfer funds to the County to pay for such projects. Such payments are considered Delegated Payments. Until June 30, 2004, the Delegated Payment was equal to the County's pass-through payment. However, after January 1, 2004, the Delegated Payment was re-defined as 20% of the proceeds of any debt secured by the Agency's non-housing tax increment revenues (excluding refunding bonds). For the fiscal year ended June 30, 2008, the pass-through payment totaled approximately $18,031,000 and Delegated Payments totaled in the amount of $40,000,000.

In August 2004, the City and the Agency filed a lawsuit seeking a judicial determination as to whether the County had breached an agreement entered into among the parties in May 2001 (the 2001 Agreement). The 2001 Agreement included provisions regarding redevelopment tax increment allocation and the application of land use procedures in County territory within the San Jose urban service area. The City and the Agency contend that under the 2001 Agreement, the County was required to abide by City land use procedures before it entered into agreements with private entities for the development of a theater on the County fairgrounds.

In April 2005, the County filed a cross compliant against the City and the Agency alleging, among other things, breach of the 2001 Agreement, breach of the 2001 Agreement's implied covenant of good faith and fair dealing, and intentional interference with prospective economic relations. The County's cross complaint alleged no specific amount of damages and sought damages and restitution according to proof. In addition a second lawsuit was filed by the County challenging the Council's approval of the North San Jose Development Policies Update. These lawsuits resulted in a settlement in November 2006.

The settlement among the City, Agency and County is that each agreed to dismiss their respective lawsuits and the Agency and/or City would pay the County a sum of $22.5 million, to be used by County on specified facilities that benefit the citizens of the City of San José. The Agency and/or City will pay the $22.5 million in three installments of $7.5 million over a three-year period, commencing on July 1, 2007. At June 30, 2008, the related liabilities in the amount of $15.0 million are recorded as part of the noncurrent obligations; estimated liability for self-insurance in the government wide financial statements. In addition, as part of the agreement, the City is required to fund up to $11 million toward certain improvements on Montague Expressway no later than June 30, 2010.

3. San José - Santa Clara Water Pollution Control Plant

The City's 2009-2013 Five-Year Capital Improvement Program includes the South Bay Water Recycling (SBWR) project, a regional water reclamation program to recycle highly treated wastewater for irrigation and industrial uses in the cities of San José, Santa Clara, and Milpitas, California. This program is part of an action plan, developed by the City and other agencies tributary to the Plant and adopted by the Regional Water Quality Control Board (RWQCB), to control the amount of effluent discharged by the Plant into San Francisco Bay.

The SBWR distribution system includes approximately 60 miles of pipe, a four million-gallon reservoir, a transmission pump station, and two booster pump stations. These facilities were constructed between 1996 and 1998 at a capital cost of approximately $140,000,000 funded by the tributary agencies, grants, and bond proceeds.

Proceeds from the 1995 Series A and B San Jose-Santa Clara Clean Water Financing Authority Sewer Revenue Bonds, which were refunded during the Fiscal Year 2005-06, (2005 Series A and B Sewer Revenue Bonds) and other funds were used to pay for the City's share of Phase I costs. The City of Santa Clara's share of Phase I costs was approximately $20,067,000. Sources of funding included credit for the City of Santa Clara's existing non-potable water reclamation distribution system, in-kind services, additional construction, and City of Santa Clara sewer utility cash reserves. Other sources of funding for Phase I included U.S. Bureau of Reclamation grants, $6,449,000 transferred in fiscal year 1995 from the Authority to the City's Wastewater Treatment Plant Capital Fund, and cash contributions from the other participating agencies.

In June 1997, the RWQCB and the City approved the Proposed Revision to the South Bay Action Plan, which described the projects necessary to reduce average dry weather effluent flow from the Plant to below 120 million gallons per day (mgd) and protect salt marsh habitat for endangered species in the South Bay as required by RWQCB Order 94-117. These projects include expanding the Phase I non-potable reuse system by extending additional piping, placing greater emphasis on water conservation programs, reducing infiltration inflow, augmenting stream flow, and creating wetlands. The estimated cost for implementing these projects was $127,500,000, of which $94,736,000 has been expended or encumbered. These estimated costs are to be funded by the City and other tributary agencies through a combination of State Revolving Fund Loans, Sewage Treatment Plant Connection Fees, federal grants, and cash contributions.

4. Federal Financial Assistance Programs

The City participates in a number of federally assisted grant programs, primarily with the Department of Housing and Urban Development, Federal Aviation Administration, the Department of Transportation, the Department of Homeland Security, the Department of Labor, and the Department of Justice. These programs are subject to program compliance audits by the grantors or their representatives.

Although the City's grant programs have been audited in accordance with the provisions of the Single Audit Act Amendments of 1996 for the fiscal year ended June 30, 2008, these programs are still subject to financial and compliance audits by Federal auditors, and to resolution of identified findings and questioned costs. At this time, the amount of expenditures, if any, which may be disallowed by the granting agencies cannot be determined.

D. Subsequent Events

1. Debt Issues

City of San José Financing Authority Lease Revenue Bonds, Series 2008E (Taxable) (Ice Centre Refunding Project). On July 3, 2008, the Authority issued $28,070,000 of Series 2008E Taxable Lease Revenue Bonds. The proceeds of the Series 2008E Bonds were used to current refund the Authority's Series 2000C (taxable) and Series 2004A (taxable) Lease Revenue Bonds (together, the "2000/2004 Bonds") issued to finance and refinance real property and improvements to the City's Ice Centre of San José. Debt service on the bonds will be paid from base rental payments received by the City from the Ice Centre operator, San José Arena Management LLC.

This refunding of variable-rate bonds with another series of variable-rate bonds constitutes a restructuring of the 2000/2004 Bonds, which had been negatively impacted by the disruptions in the financial markets related to both auction rate securities and rating agency downgrades of bond insurers. The Series 2008E Bonds financing structure eliminated the bond insurance which provided credit enhancement to the 2000/2004 Bonds and replaced it with a direct-pay letter of credit. The 2000/2004 Bonds were redeemed on July 3, 2008.

The Series 2008E Bonds, which are supported by an irrevocable direct-pay letter of credit provided by Bank of America and the California State Teachers' Retirement System, bear interest at weekly variable rates and have a final maturity date of June 1, 2025.

City of San José Financing Authority Lease Revenue Bonds, Series 2008B (Civic Center Garage Refunding Project). On July 10, 2008, the Authority issued $36,580,000 of Series 2008B Lease Revenue Bonds. The proceeds of the Series 2008B Bonds were used to current refund the portion of the Authority's Lease Revenue Commercial Paper Notes issued as an interim financing mechanism to finance land acquisition and construction of the Civic Center Employee Parking Garage and certain improvements to the Civic Center. Debt service on the Series 2008B bonds will be paid from the General Fund, special revenue funds, and capital project funds.

This refunding of variable-rate commercial paper notes with a series of variable-rate bonds provides long-term financing for the Civic Center Garage. A note repayment fund for the Lease Revenue Commercial Paper Notes, in the amount of $32,528,000 was funded from the Series 2008B bond proceeds and was used to current refund a portion of the outstanding Lease Revenue Commercial Paper Notes when those notes matured on July 11, 2008.

The Series 2008B Bonds, which are supported by an irrevocable direct-pay letter of credit provided by Bank of America and the California State Teachers' Retirement System, bear interest at weekly variable rates and have a final maturity date of June 1, 2039.

City of San José Financing Authority Lease Revenue Bonds, Series 2008A (Civic Center Refunding Project). On August 14, 2008, the Authority issued $60,310,000 of Series 2008A Lease Revenue Bonds. The proceeds of the Series 2008A Bonds were used to current refund the Authority's Series 2002C Lease Revenue Bonds issued to finance a portion of the costs of the City Hall project. Debt service on the Series 2008A bonds will be paid from the General Fund, special revenue funds, and capital project funds.

This refunding of variable-rate bonds with another series of variable-rate bonds constitutes a restructuring of the Series 2002C Bonds, which had been negatively impacted by the disruptions in the financial markets related to auction rate securities and rating agency downgrades of bond insurers. The Series 2008A Bonds financing structure eliminated the bond insurance which provided credit enhancement to the Series 2002C Bonds and replaced it with a direct-pay letter of credit. The Series 2002C Bonds were redeemed on August 14, 2008.

The Series 2008A Bonds, which are supported by an irrevocable direct-pay letter of credit provided by The Bank of Nova Scotia and the California State Teachers' Retirement System, bear interest at weekly variable rates and have a final maturity date of June 1, 2039.

2. Recent Changes in the Economic Environment and its Impact to the City

The recent turmoil in the financial market has been unprecedented. In September 2008, the U.S. Treasury placed government sponsored enterprises Fannie Mae (Federal National Mortgage Association) and Freddie Mac (Federal Home Loan Mortgage Corporation) into conservatorship and committed to provide as much as $100 billion to each company to backstop any shortfalls in capital through 2009, which protected the principal and interest payments on their debt (bonds issued). In addition, the federal government recently assumed control of American International Group Inc. (AIG), the largest insurance company in the U. S.; Lehman Brothers Holdings Inc., the 4th largest investment bank in the U.S. filed for bankruptcy; and Washington Mutual Inc. was seized by government regulators and its branches and assets sold to JPMorgan Chase & Co. On October 3, 2008, the President of the United States signed into law the $700 billion Emergency Economic Stabilization Act of 2008 in an effort to address the economic crisis.

The fair value of the Police & Fire Department Retirement Plan's and the Federated Employees' Retirement System's (collectively "the Retirement Systems") current equity and fixed income investments related to AIG, Lehman Brothers Holdings Inc., and Washington Mutual Inc. are approximately $19.7 million or 0.5% of the fair value of the Retirement Systems' total portfolio of approximately $4.0 billion, excluding securities lending and transactions in transit, as of September 30, 2008 (based on available information). The fair value of the Retirement Systems' portfolio as of June 30, 2008, excluding securities lending and transactions in transit, decreased by 7.0 percent during the quarter ended September 30, 2008 (based on available information).

As is the case with most retirement systems, the Retirement Systems are exposed to general market risk. In a pension plan context, the market risk is the risk that the rate of return earned on the pension plan assets could be below the actuarially assumed rate of return, which is 8.0% for the Police & Fire Department Retirement Plan and 8.25% for the Federated Employees' Retirement System. This general market risk is reflected in asset valuations fluctuating with market volatility. Any impact from market volatility on the Retirement Systems depends in large measure on how deep the market downturn is, how long it lasts, and how it fits within fiscal year reporting periods. Market risk could impact the financial condition of the Retirement Systems and the City's required contribution to the Retirement Systems.

With respect to potential loss of principal on any of the City's investments, the City's investment policy limits the composition of the holdings within the City's Equity in Pooled Cash and Investments held in City Treasury. The City's review of these holdings as of September 30, 2008 confirms no investments with AIG, Lehman Brothers Holdings, Inc., or Washington Mutual Inc.. The Finance Department's investment staff continues to focus investment decisions in accordance with the City Council Investment Policy's primary investment priorities of safety, liquidity and yield; in that order.

Required Supplementary Information

City of San José
General Fund
Schedule of Revenues, Expenditures and Changes in Fund Balance-Budget and Actual
For the Year Ended June 30, 2008
($000's)

	Budgeted Amounts Original	Budgeted Amounts Final	Actual Amounts Budgetary Basis Variance with Final Budget Over (Under)	Actual Amounts Budgetary Basis	Budgetary to GAAP Differences	Actual Amounts GAAP Basis	
REVENUES							
Taxes:							
Property	$ 198,154	203,454	264	203,718	-	203,718	
Sales	152,636	152,636	1,366	154,002	-	154,002	
Utility	79,141	82,141	114	82,255	-	82,255	
State of California in-lieu	7,898	9,442	(198)	9,244	-	9,244	
Franchise	39,032	40,832	232	41,064	-	41,064	
Other	8,988	8,988	572	9,560	-	9,560	
Licenses, permits and fines	87,197	90,507	(851)	89,656	-	89,656	
Intergovernmental	22,020	20,160	(7,398)	12,762	-	12,762	
Charges for current services	29,157	29,481	1,052	30,533	-	30,533	
Investment income	15,496	18,339	476	18,815	7,337	26,152	(1)
Other revenues	29,131	33,461	2,375	35,836	(374)	35,462	(4)
Total revenues	668,850	689,441	(1,996)	687,445	6,963	694,408	
EXPENDITURES							
Current:							
General government	134,480	133,125	(36,166)	96,959	(10,052)	86,907	(2), (3)
Public safety	396,734	434,867	(13,486)	421,381	(5,126)	416,255	(2)
Capital maintenance	74,409	91,013	(23,322)	67,691	(17,013)	50,678	(2)
Community services	157,501	162,465	(15,906)	146,559	(4,681)	141,878	(2)
Sanitation	3,196	2,638	(257)	2,381	(485)	1,896	(2)
Capital outlay	684	6,496	(528)	5,968	(4,499)	1,469	(2)
Total expenditures	767,004	830,604	(89,665)	740,939	(41,856)	699,083	
Excess (deficiency) of revenues over expenditures	(98,154)	(141,163)	87,669	(53,494)	48,819	(4,675)	
OTHER FINANCING SOURCES (USES)							
Loan proceeds	-	-	-	-	(374)	374	(4)
Transfers in	38,112	39,165	27	39,192	-	39,192	
Transfers out	(35,120)	(38,355)	-	(38,355)	-	(38,355)	
Total other financing sources (uses)	2,992	810	27	837	(374)	1,211	
Net change in fund balances	(95,162)	(140,353)	87,696	(52,657)	48,445	(3,464)	
Fund balances - beginning	247,630	247,630	-	247,630	32,967	280,597	
Beginning encumbrance	-	-	-	28,678	-	-	
Fund balances - ending	$ 152,468	107,277	87,696	223,651	81,412	277,133	

Explanation of differences:
(1) Gain or loss in fair value of investments are not formally budgeted transactions.
(2) Encumbrances of funds for which formal budget are prepared.
(3) Expenditures and repayments that increase and decrease certain loan receivables for which formal budgets are prepared.
(4) Loan proceeds are budgetary reclassed as other revenue

See accompanying notes to the required supplementary information.

City of San José
Housing Activities
Schedule of Revenues, Expenditures and Changes in Fund Balance-Budget and Actual
For the Year Ended June 30, 2008
($000's)

	Budgeted Amounts Original	Budgeted Amounts Final	Actual Amounts Budgetary Basis Variance with Final Budget Over (Under)	Actual Amounts Budgetary Basis	Budgetary to GAAP Differences	Actual Amounts GAAP Basis	
REVENUES							
Intergovernmental	$ 13,931	29,308	(17,995)	11,313	-	11,313	
Charges for current services			6	6	-	6	
Investment income	9,140	9,140	8,652	17,792	868	18,660	(1)
Other revenues	8,486	19,610	(1,508)	18,102	(8,280)	9,822	(3)
Total revenues	31,557	58,058	(10,845)	47,213	(7,412)	39,801	
EXPENDITURES							
Current							
Capital maintenance		130	(86)	44	-	44	
Community services	116,149	163,826	(48,760)	115,066	(113,446)	1,620	(2), (3)
Total expenditures	116,149	163,956	(48,846)	115,110	(113,446)	1,664	
Excess (deficiency) of revenues over expenditures	(84,592)	(105,898)	38,001	(67,897)	106,034	38,137	
OTHER FINANCING SOURCES (USES)							
Capital lease financing proceeds							
Transfers in	52,800	80,493	(29,650)	50,843	-	50,843	
Transfers out	(19,573)	(19,573)		(19,573)	1,000	(19,572)	
Total other financing sources (uses)	33,227	60,920	(29,650)	31,270	1	31,271	
Net change in fund balances	(51,365)	(44,978)	8,351	(36,627)	106,035	69,408	
Fund balance - beginning	11,020	11,020	-	11,020	242,465	253,485	
Add beginning encumbrance balance	-	-	-	39,284	-	-	
Fund balances - ending	$ (40,345)	(33,958)	8,351	13,677	348,500	322,893	

Explanation of differences:
(1) Gain or loss in fair value of investments are not formally budgeted transactions.
(2) Encumbrances of funds for which formal budget are prepared.
(3) Expenditures and repayments that increase and decrease certain loan receivables for which formal budgets are prepared.

See accompanying notes to the required supplementary information.

Required Supplementary Information

June 30, 2008

Schedules of Funding Progress
($000's)

Police and Fire Department Retirement Plan - Defined Benefit Pension Plan

Actuarial Valuation Date (4)		Actuarial Value of Assets (1)	Actuarial Accrued Liability (AAL) (2)	Unfunded (Overfunded) AAL	Funded Ratio	Annual Covered Payroll (3)	(Overfunded) Unfunded AAL as a Percentage of Covered Payroll
6/30/03	$	1,826,287	1,823,200	(3,087)	100%	202,222	(2)%
6/30/05		1,983,090	2,027,432	44,342	98%	210,018	21%
6/30/07		2,365,790	2,372,386	6,596	100%	227,734	3%

Federated City Employees' Retirement System - Defined Benefit Pension Plan

Actuarial Valuation Date (4)		Actuarial Value of Assets (1)	Actuarial Accrued Liability (AAL) (2)	Unfunded AAL	Funded Ratio	Annual Covered Payroll (3)	Unfunded AAL as a Percentage of Covered Payroll
6/30/03	$	1,280,719	1,311,691	30,972	98%	292,961	11%
6/30/05		1,384,454	1,711,370	326,916	81%	286,446	114%
6/30/07		1,622,851	1,960,943	338,092	83%	291,405	116%

(1) Excludes accounts payable and postemployment healthcare plan assets.
(2) Excludes postemployment healthcare liability.
(3) Annual covered payroll represents the actuarial estimate of annual covered payroll for the subsequent year.
(4) Actuarial valuations have been performed biennially through June 30, 2007.

Police and Fire Department Retirement Plan - Postemployment Healthcare Benefit Plan

Actuarial Valuation Date		Actuarial Value of Assets	Actuarial Accrued Liability (AAL)	Unfunded AAL	Funded Ratio	Annual Covered Payroll	Unfunded AAL as a Percentage of Covered Payroll
6/30/06	$	38,381	851,217	812,836	5%	218,521	372%

Federated City Employees' Retirement System - Postemployment Healthcare Benefit Plan

Actuarial Valuation Date		Actuarial Value of Assets	Actuarial Accrued Liability (AAL)	Unfunded AAL	Funded Ratio	Annual Covered Payroll	Unfunded AAL as a Percentage of Covered Payroll
6/30/06	$	81,288	702,939	621,651	12%	275,559	226%

Notes to Required Supplementary Information

June 30, 2008

I. Budgetary Information

The adopted budget represents the financial and organizational plan by which the policies and programs approved by the City Council will be implemented. It includes: (1) the programs, projects, services and activities to be provided during the fiscal year; (2) estimated revenues available to finance the operating plan; and (3) the estimated spending requirements of the operating plan. The City Charter requires that the City establish a budgetary system for general operations and prohibits expending funds for which there is no legal appropriation.

Annual budgets are prepared for the General Fund and all special revenue funds except for the following:

- Developer Fees
- William F. Prusch, Jr.
- Special Assessment Special Services
- Emergency Reserve

The annual appropriation ordinance adopts the budget at the appropriation level by expenditure category (personal services, nonpersonal) within departments. Accordingly, the lowest level of budgetary control exercised by the City Council is the appropriation level within a department. The City's legal level of budgetary control is so detailed that it is not practical to demonstrate compliance within the CAFR itself. As a result, the City prepares a separate report to demonstrate compliance with its legal level of budgetary control.

Capital project budgets are based on a project time frame rather than a fiscal year time frame and therefore are not included. Debt Service Funds appropriations were implicitly adopted by the Council when the formal bond resolutions were approved.

II. Budgetary Results Reconciled to GAAP

The budgetary process is based upon accounting for certain transactions on a basis other than the accounting principles generally accepted in the United States (GAAP) basis. The results of operations are presented in the accompanying budget and actual comparison schedules in accordance with the budgetary process (budgetary basis) to provide a meaningful comparison with the budget.

The major differences between the budgetary basis actual and GAAP basis are as follows:

- Year-end encumbrances are recognized as the equivalent of expenditures in the budgetary basis financial statements, while encumbered amounts are not recognized as expenditures on the GAAP basis until the equipment, supplies, or services are received.

- Certain loan transactions are recognized as expenditures for the budgetary basis but not for the GAAP basis. When these loans are made, they are recorded as receivables for the GAAP basis and as expenditures for the budgetary basis. When loan repayments are received, they are recorded as reductions to receivables for the GAAP basis, but are recognized as revenues for the budgetary basis.

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Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

City Council
City of San José, California

We have audited the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of San José, California (the City) as of and for the year ended June 30, 2008, which collectively comprise the City's basic financial statements, and have issued our report thereon dated October 8, 2008. As discussed in Note I.E. to the financial statements, the City adopted the provisions of Governmental Accounting Standards Board (GASB) Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions* and GASB Statement No. 50, *Pension Disclosures—an amendment of GASB Statements No. 25 and No. 27*. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting
In planning and performing our audit, we considered the City's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the City's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the City's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified a deficiency in internal control over financial reporting that we consider to be a significant deficiency.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the City's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the City's financial statements that is more than inconsequential will not be prevented or detected by the City's internal control. We consider the deficiency described in the accompanying federal awards schedule of findings and questioned costs as item 2008-A to be a significant deficiency in internal control over financial reporting.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, we believe that the significant deficiency described above is not a material weakness.

Compliance and Other Matters
As part of obtaining reasonable assurance about whether the City's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

We noted certain matters that we reported to management of the City in a separate letter dated October 8, 2008.

The City's response to the finding identified in our audit is described in the accompanying federal awards schedule of findings and questioned costs. We did not audit the City's response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of the City Council, the City's management, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Macias Gini & O'Connell LLP
Certified Public Accountants

Walnut Creek, California
October 8, 2008

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Independent Auditor's Report on Compliance with Requirements Applicable to Each Major Program and the Passenger Facility Charges Program and on Internal Control over Compliance in Accordance with OMB Circular A-133

City Council
City of San José, California

Compliance

We have audited the compliance of the City of San José, California (the City) with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) *Circular A-133 Compliance Supplement* and the *Passenger Facility Charge Audit Guide for Public Agencies* issued by the Federal Aviation Administration *(PFC Guide)* that are applicable to each of its major federal programs and to the passenger facility charges program, respectively, for the year ended June 30, 2008. The City's major federal programs are identified in the summary of auditor's results section of the accompanying federal awards schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs and the passenger facility charges program is the responsibility of the City's management. Our responsibility is to express an opinion on the City's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*; and the *PFC Guide*. Those standards, OMB Circular A-133, and the *PFC Guide* require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program and on the passenger facility charges program occurred. An audit includes examining, on a test basis, evidence about the City's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of the City's compliance with those requirements.

In our opinion, the City complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs and to the passenger facility charges program for the year ended June 30, 2008.

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Internal Control Over Compliance

The management of the City is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs and the passenger facility charges program. In planning and performing our audit, we considered the City's internal control over compliance with the requirements that could have a direct and material effect on a major federal program and the passenger facility charges program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the City's internal control over compliance.

A *control deficiency* in an entity's internal control over compliance exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect noncompliance with a type of compliance requirement of a federal program on a timely basis. A *significant deficiency* is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to administer a federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by the entity's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that material noncompliance with a type of compliance requirement of a federal program or the passenger facility charges program will not be prevented or detected by the entity's internal control.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

This report is intended solely for the information and use of the City Council, the City's management, the Federal Aviation Administration, federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Macias Gini & O'Connell LLP

Certified Public Accountants
Walnut Creek, California

October 8, 2008

CITY OF SAN JOSE, CALIFORNIA
Schedule of Expenditures of Federal Awards
Year Ended June 30, 2008

Federal Grantor/Pass-Through Grantor/Program	Federal Catalog Number	Grant Identifying Number	Grant Amount	Expenditures Federal Grant	Expenditures Other
U.S. Department of Commerce					
Economic Adjustment Assistance	11.307	07-39-02866	$ 345,000	$ 45,106	
Economic Adjustment Assistance	11.307	07-79-05812	200,000	32,025	$ 32,025
Total U.S. Department of Commerce			545,000	77,131	32,025
U.S. Department of Housing and Urban Development					
Community Development Block Grants/ Entitlement Grants	14.218	B05-06-07 MC-06-0021	32,079,121	11,719,528	-
Community Development Block Grants/ Entitlement Grants	14.218	Prior Year Ending Loan Balance	-	6,966,710	-
Subtotal Community Development Block Grants/Entitlement Grants			32,079,121	18,686,238	-
Emergency Shelter Grants Program	14.231	S06-MC-060021	441,400	19,949	-
Emergency Shelter Grants Program	14.231	S07-MC-060021	444,347	426,124	-
Subtotal Emergency Shelter Grants Program			885,747	446,073	-
Home Investment Partnerships Program	14.239	M01-02 MC06215	8,637,000	320,809	-
Home Investment Partnerships Program	14.239	M03-04 MC06215	10,321,912	1,351,400	-
Home Investment Partnerships Program	14.239	M05-06 MC06215	9,185,083	3,669,291	-
Home Investment Partnerships Program	14.239	M07-08 MC06215	8,612,627	953,790	-
Home Investment Partnerships Program	14.239	Prior Year Ending Loan Balance	-	36,305,529	-
Subtotal Home Investment Partnerships Program			36,756,622	42,600,819	-
Housing Opportunities for Persons with AIDS	14.241	CA-39-H05-F069	736,000	14,605	-
Housing Opportunities for Persons with AIDS	14.241	CA-39-H06-F069	738,000	241,486	-
Housing Opportunities for Persons with AIDS	14.241	CA-39-H07-F069	739,000	617,701	-
Housing Opportunities for Persons with AIDS	14.241	CA-H99-0032	1,346,000	29,649	-
Housing Opportunities for Persons with AIDS	14.241	CA-H103-0001	1,323,800	40,661	-
Housing Opportunities for Persons with AIDS	14.241	CA-H107-0003	1,226,500	362,667	-
Subtotal Housing Opportunities for Persons with AIDS			6,109,300	1,306,769	-
Community Development Block Grants/ Brownfields Economic Development Initiative	14.246	B-04-BD-06-0024	2,057,253	665,313	-
Community Development Block Grants_Section 108 Loan Guarantees	14.248	B-04-MC-06-0021	25,837,640	445,127	1,059,537
Economic Development Initiative - Special Projects, Neighborhood Initiative and Miscellaneous Grants	14.251	B05SPCCA0727	96,224	53,888	-
Total U.S. Department of Housing and Urban Development			103,821,907	64,204,227	1,059,537

See accompanying notes to the Schedule of Expenditures of Federal Awards and Schedule of Revenues and Expenditures of Passenger Facility Charges

CITY OF SAN JOSE, CALIFORNIA
Schedule of Expenditures of Federal Awards (Continued)
Year Ended June 30, 2008

Federal Grantor/Pass-Through Grantor/Program	Federal Catalog Number	Grant Identifying Number	Grant Amount	Expenditures Federal Grant	Expenditures Other
U.S. Department of Justice					
Part D - Research, Evaluation, Technical Assistance and Training	16.542	2003-MC-CX-K001	1,099,491	228,981	-
Title V_Delinquency Prevention Program	16.548	2005JLFX0158	246,661	10,528	-
Edward Byrne Memorial State and Local Law Enforcement Assistance Discretionary Grants Program	16.580	2005-VT-BX-1155	225,000	154,042	817
Edward Byrne Memorial State and Local Law Enforcement Assistance Discretionary Grants Program	16.580	2007-DD-BX-0005	394,890	124,630	-
Subtotal Edward Byrne Memorial State and Local Law Enforcement Assistance Discretionary Grants Program			619,890	278,672	817
Community Capacity Development Office	16.595	2006-WS-Q6-0046	225,000	183,005	-
Community Capacity Development Office	16.595	2007-WS-Q7-0046	200,000	18,913	-
Subtotal Community Capacity Development Office			425,000	201,918	-
Public Safety Partnership and Community Policing Grants	16.710	2003INWX1	3,692,162	945,451	315,149
Edward Byrne Memorial Justice Assistance Grant Program	16.738	DC07180430	132,552	132,552	-
Edward Byrne Memorial Justice Assistance Grant Program	16.738	2005-DJ-BX-1720	395,115	141,290	-
Edward Byrne Memorial Justice Assistance Grant Program	16.738	2006-DJ-BX-0883	270,752	254,797	-
Edward Byrne Memorial Justice Assistance Grant Program	16.738	2007-DJ-BX-0531	298,310	82,257	-
Subtotal Edward Byrne Memorial Justice Assistance Grant Program			1,096,729	610,896	-
Convicted Offender and/or Arrestee DNA Backlog Reduction Program	16.748	2007-WP-BX-0008	250,000	138,302	72,775
Total U.S. Department of Justice			7,429,933	2,414,748	388,741
U.S. Department of Labor					
Pass-through State of California, Employment Development Department:					
Workforce Investment Act (WIA) Cluster:					
WIA Dislocated Workers	17.260	R692502	19,821	17,637	-
WIA Adult Program	17.258	R760350	3,201,513	1,214,532	-
WIA Youth Activities	17.259	R760350	4,120,814	2,058,896	-
WIA Dislocated Workers	17.260	R760350	2,456,752	1,825,941	-
WIA Adult Program	17.258	R865486	3,366,005	2,622,100	-
WIA Youth Activities	17.259	R865486	3,549,446	1,342,687	-
WIA Dislocated Workers	17.260	R865486	3,549,373	2,268,596	-
Subtotal WIA Adult/Youth/Dislocated Workers Programs			20,263,724	11,350,389	-
Total U.S. Department of Labor			20,263,724	11,350,389	-

See accompanying notes to the Schedule of Expenditures of Federal Awards and Schedule of Revenues and Expenditures of Passenger Facility Charges

CITY OF SAN JOSE, CALIFORNIA

Schedule of Expenditures of Federal Awards (Continued)

Year Ended June 30, 2008

Federal Grantor/Pass-Through Grantor/Program	Federal Catalog Number	Grant Identifying Number	Grant Amount	Expenditures: Federal Grant	Expenditures: Other
U.S. Department of Transportation					
Federal Aviation Administration:					
Airport Improvement Program	20.106	3-06-0226-57	4,000,000	285,636	224,404
Airport Improvement Program	20.106	3-06-0226-61	3,400,000	883,153	101,664
Airport Improvement Program	20.106	3-06-0226-62	14,659,598	414,355	100,118
Airport Improvement Program	20.106	3-06-0226-63	6,000,000	4,632,276	1,017,455
Airport Improvement Program	20.106	3-06-0226-64	1,000,000	733,151	176,579
Airport Improvement Program	20.106	3-06-0226-66	2,467,466	2,467,466	-
Airport Improvement Program	20.106	3-06-0226-67	6,000,000	2,408,744	648,118
Airport Improvement Program	20.106	3-06-0226-68	870,372	452,050	94,821
Airport Improvement Program	20.106	3-06-0226-70	3,000,000	534,604	132,713
Subtotal Airport Improvement Program			41,397,436	12,811,435	2,495,872
Recreational Trails Program					
Pass-through California Department of Transportation:					
SAFETEA-LU Trail: Bay Reach 7/9	20.219	SCL 050082 HPLUL-5005(086)	675,000	148,074	7,779
Highway Planning and Construction					
Pass-through California Department of Transportation:					
Federal-Aid Highway Program					
SVSC ITS Enhancement	20.205	ITS99-5005(058)	1,187,204	53,488	53,488
SVSC West Corridor - Stevens Creek - CMAQ	20.205	CML-5005(064)	4,748,000	1,968,202	-
TEA-21-ITS: New CC TMC (Web II)	20.205	ITS03-5005(073)	579,123	108,919	108,919
Federal Street Maintenance	20.205	SCL 050028	16,300,666	4,398,820	2,319,458
HBRR Seismic Bridge Retrofit - Julian Street	20.205	BRLZ 5005(080)	769,443	164,313	26,771
HBRR Seismic Bridge Retrofit - Southwest Expressway	20.205	BRLZ 5005(079)	671,058	116,535	22,819
HBRR Seismic Bridge Retrofit - William Street	20.205	BRLZ 5005(081)	521,795	129,771	19,336
Subtotal pass-through California Department of Transportation			24,777,289	6,940,048	2,550,791
Pass-through the Metropolitan Transportation Commission					
HBRR - Willow Glen Way Bridge	20.205	BRLZ 5005(038)	3,428,354	380,507	104,248
Subtotal Highway Planning and Construction			28,205,643	7,320,555	2,655,039
State and Community Highway Safety					
Pass-through the California Department of Transportation:					
DUI and Seat Belt Safety Program	20.600	AL0574	637,915	19,393	-
Sobriety Checkpoint Program for Local Law Enforcement Agencies	20.600	SC074302	54,932	12,897	-
2008 Sobriety Checkpoint Mini-Grant	20.600	SC08372	91,814	48,940	-
07-08 Click It or Ticket Grant	20.600	CT-08372	15,000	13,912	-
Subtotal State and Community Highway Safety			799,661	95,142	-
Total U.S. Department of Transportation			71,077,740	20,375,206	5,158,690

See accompanying notes to the Schedule of Expenditures of Federal Awards and Schedule of Revenues and Expenditures of Passenger Facility Charges

Federal Grantor/Pass-Through Grantor/Program	Federal Catalog Number	Grant Identifying Number	Grant Amount	Expenditures: Federal Grant	Expenditures: Other
National Endowment for the Humanities					
Pass-through the California State Library					
Grants to States Program:					
Staff Education Grant	45.310	40-6649	1,180	-	1,100
Staff Education Grant	45.310	40-6830	4,587	4,587	-
ELF Storytime and Play	45.310	40-6919	25,000	25,000	-
Subtotal Grants to States Program			30,767	29,587	1,100
Total National Endowment for the Humanities			30,767	29,587	1,100
Environmental Protection Agency					
Congressionally Mandated Projects	66.202	XP-96942501-0	673,000	70,886	214,314
Total Environmental Protection Agency			673,000	70,886	214,314
U.S. Department of Health and Human Services					
Special Programs for the Aging_Title III, Part B _ Grants for Supportive Services and Senior Centers	93.044	Contract 1200	286	286	-
Nutrition Services Incentive Program	93.053	Contract 1200	146,000	39,220	-
Total U.S. Department of Health and Human Services			146,286	39,506	-
Corporation for National and Community Services					
Retired and Senior Volunteer Program	94.002	06SRPCA017	277,855	94,236	243,827
Senior Companion Program	94.016	06SCPCA007	260,618	130,309	174,053
Total Corporation for National and Community Services			538,473	224,545	417,880
U.S. Department of Homeland Security					
National Explosives Detection Canine Team Program	97.072	DTSA20-03-H-01015	1,019,186	100,000	442,566
National Explosives Detection Canine Team Program	97.072	HSTS0208HCAN452	100,500	100,000	76,805
Subtotal National Explosives Detection Canine Team Program			1,119,686	200,000	519,371
Law Enforcement Officer Reimbursement Agreement Program	97.090	HSTS0208HSLR344	429,094	289,093	411,760
Pass-through the County of Santa Clara					
Emergency Management Performance Grants	97.042	2006-8	129,292	129,292	129,292
Emergency Management Performance Grants	97.042	2007-6	130,731	130,731	130,731
Subtotal Emergency Management Performance Grants			260,023	260,023	260,023

See accompanying notes to the Schedule of Expenditures of Federal Awards and Schedule of Revenues and Expenditures of Passenger Facility Charges

CITY OF SAN JOSE, CALIFORNIA
Schedule of Expenditures of Federal Awards (Continued)
Year Ended June 30, 2008

Federal Grantor/Pass-Through Grantor/Program	Federal Catalog Number	Grant Identifying Number	Grant Amount	Expenditures: Federal Grant	Expenditures: Other
U.S. Department of Homeland Security (continued)					
Homeland Security Cluster					
Pass-through the California Governor's Office of Homeland Security					
FY 05 Urban Areas Security Initiative	97.008	2005-0015	6,019,311	920,710	-
Pass-through the City and County of San Francisco					
FY 06 Urban Areas Security Initiative	97.008	2006-0071	1,000,000	1,000,000	-
FY 06 Urban Areas Security Initiative	97.008	n/a	3,466,667	3,329,100	-
FY 07 Urban Areas Security Initiative	97.008	2006-0071	1,000,000	264,152	-
FY 07 Urban Areas Security Initiative	97.008	n/a	2,860,000	183,339	-
Subtotal pass-through the City and County of San Francisco			8,326,667	4,776,591	-
Pass-through the County of Santa Clara					
FY 06 Urban Areas Security Initiative	97.008	n/a	4,848	4,848	-
FY 07 Urban Areas Security Initiative	97.008	n/a	18,728	12,131	-
FY 06 Metropolitan Medical Response System	97.067	2006-0071	232,329	217,608	-
FY 06 State Homeland Security Grant program	97.067	n/a	45,444	45,444	-
Subtotal pass-through the County of Santa Clara			301,349	280,031	-
Subtotal Homeland Security Cluster			14,647,327	5,977,332	-
Total U.S. Department of Homeland Security			16,456,130	6,726,448	1,191,154
Total Federal Awards			$ 220,982,960	$ 105,512,673	$ 8,463,441

See accompanying notes to the Schedule of Expenditures of Federal Awards and Schedule of Revenues and Expenditures of Passenger Facility Charges

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CITY OF SAN JOSE, CALIFORNIA

Schedule of Revenues and Expenditures of Passenger Facility Charges

Year Ended June 30, 2008

Passenger Facility Charges Project Number/Description		Identifying Number	Passenger Facility Charges Project Amount	Expenditures	Revenue Recognized
Total Passenger Facility Charges Collection Revenues					
Passenger Facility Charges Collections					$ 21,223,684
Interest Earned on PFC Program					5,104,288
Passenger Facility Charges Projects					
#1	Communication Center Upgrade	92-01-C-00-SJC	$ 500,000	$ -	-
#2	Fire Truck Replacement	92-01-C-00-SJC	599,826	-	-
#3	Handlift Replacement	92-01-C-00-SJC	103,000	-	-
#4	Noise Attenuation	92-01-C-06-SJC	47,171,000	-	-
#5	Noise Monitoring System Upgrade	92-01-C-00-SJC	184,000	-	-
#6	Noise Remedy/Land Acquisition	92-01-C-00-SJC	5,133,000	-	-
#7	Security Access Control System	92-01-C-07-SJC	1,032,000	-	-
#40a	Runway 30L Reconstruction	98-06-I-00-SJC	72,022,700	-	-
#40b	Runway 30L Extension	98-06-I-00-SJC	38,671,724	-	-
#41	Aircraft Noise & Operation Management System	99-07-C-00-SJC	100,000	-	-
#42	Emergency Command Post Relocation & Equipment	99-07-C-00-SJC	150,000	-	-
#43	Interim Federal Inspection Service (FIS) Facility	99-08-C-02-SJC	36,879,750	(928)	-
#44	Airfield Lighting Control System	99-07-C-00-SJC	200,000	-	-
#46	Ewert Road Improvements	99-07-C-00-SJC	408,000	-	-
#47	Skyport Access to Airport Boulevard	99-07-C-00-SJC	1,083,000	-	-
#48	Taxiway Y Pavement Reconstruction	99-07-C-01-SJC	2,100,000	-	-
#49	Transportation Access Plan, Terminal Area Concept	99-07-C-01-SJC	1,050,000	-	-
#50	Terminal C Ramp Lighting Improvement	99-07-C-00-SJC	37,000	-	-
#51	Acoustical Treatment of Four Eligible Schools	99-07-C-01-SJC	7,500,000	-	-
#52	Taxiway Z - Apron Reconstruction (Phase II)	00-11-C-00-SJC	825,000	-	-
#53	Terminal C Fire Protection	00-11-C-00-SJC	580,000	-	-
#54	Fiber Optic Cable to ARC & Fire Station 29	00-11-C-00-SJC	85,000	-	-
#55	Green Island Bridge	00-11-C-00-SJC	825,000	-	-
#56	Replacement of AACS and CCTV	00-11-C-00-SJC	4,075,000	-	-
#57	Skyport Grade Separation	00-11-C-00-SJC	18,218,000	-	-
#58	Terminal Drive Improvements	00-11-C-00-SJC	1,146,000	-	-
#59	Replacement of PASSUR	00-11-C-00-SJC	221,000	-	-
#60	Terminal C Restroom	00-11-C-00-SJC	2,485,000	-	-
#61	Interim Air Cargo Ramp Extension	00-11-C-01-SJC	1,100,000	-	-
#62	Runway 30R/12L Reconstruction	00-11-C-00-SJC	84,105,103	-	-
#63	Noise Attenuation Category II & III	00-11-C-00-SJC	4,500,000	12,242	-
#64	Taxiway Y Extension	00-11-C-00-SJC	12,890,000	-	-
#65	Extended Noise Attenuation	02-13-C-00-SJC	61,589,000	2,969,654	-
#66	Taxiway Y Reconstruction	04-14-C-00-SJC	39,131,000	(404,459)	-
#67	Terminal B - North Concourse	06-15-C-00-SJC	495,095,000	38,696,000	-
	Total Passenger Facility Charge Projects		$ 941,795,103	$ 41,272,509	$ 26,327,972

See accompanying notes to the Schedule of Expenditures of Federal Awards and Schedule of Revenues and Expenditures of Passenger Facility Charges

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CITY OF SAN JOSE, CALIFORNIA

Notes to the Schedule of Expenditures of Federal Awards and
Schedule of Revenues and Expenditures of Passenger Facility Charges

Year Ended June 30, 2008

(1) GENERAL

The accompanying schedule of expenditures of federal awards (SEFA) presents the activity of the federal award programs of the City of San José, California (the City). The City's reporting entity is defined in Note I to its basic financial statements. The SEFA includes all federal awards received directly from federal agencies and federal awards passed-through other governmental agencies. In addition, the SEFA includes local, state and other expenditures matched along with the federal award expenditures.

The schedule of revenues and expenditures of passenger facility charges (PFCs) presents only the activity of the passenger facility charges program of the Norman Y. Mineta San José International Airport (Airport), an enterprise fund of the City. PFCs are fees imposed on enplaned passengers by the Airport for the purpose of generating revenue for Airport projects that increase capacity, increase safety, mitigate noise impact and enhance competition between and among air carriers in accordance with Federal Aviation Administration approvals.

(2) BASIS OF PRESENTATION

The accompanying schedules are presented using the modified accrual basis of accounting for program expenditures accounted for in the governmental funds and the accrual basis of accounting for program expenditures accounted for in the proprietary funds as described in Note I to the City's basic financial statements, with the exception of the City's loan programs (see Note 6).

(3) RELATIONSHIP TO THE BASIC FINANCIAL STATEMENTS

Expenditures of federal awards and PFCs are reported in the City's basic financial statements as expenditures in the general, special revenue and capital projects funds and as expenses for non-capital expenditures and as additions to capital assets for capital related expenditures in the enterprise funds. Federal award expenditures agree or can be reconciled with the amounts reported in the City's basic financial statements.

(4) RELATIONSHIP TO FEDERAL FINANCIAL REPORTS

Amounts reported in the SEFA and Schedule of Revenues and Expenditures of Passenger Facility Charges agree to or can be reconciled with the amounts reported in the related federal financial reports.

(5) AMOUNTS PROVIDED TO SUBRECIPIENTS

Included in the total expenditures of federal awards are the following amounts passed through to subrecipients:

Program Title	Federal Catalog Number	Amount Provided to Subrecipients
Community Development Block Grants/ Entitlement Grants	14.218	$2,907,669
Emergency Shelter Grants Program	14.231	353,435
Housing Opportunities for Persons with AIDS	14.241	1,216,134
Workforce Investment Act (WIA) Adult Program	17.258	1,299,874
Workforce Investment Act (WIA) Youth Activities	17.259	1,168,609
Workforce Investment Act (WIA) Dislocated Workers	17.260	1,369,874
Highway Planning and Construction	20.205	332,172
Urban Areas Security Initiative	97.008	10,914

(6) LOANS OUTSTANDING

The City participates in certain federal award programs that sponsor revolving loan programs, which are administered by the City. These programs maintain servicing and trust arrangements with the City to collect loan repayments. The funds are returned to the programs upon repayment of the principal and interest. The federal government has imposed certain continuing compliance requirements with respect to the loans under the Community Development Block Grants/Entitlement Grants (CDBG) and the HOME Investment Partnership Program (HOME). In accordance with Subpart B, Section 205 of the Office of Management and Budget Circular A-133, the City has reported the outstanding balance of loans from previous years that have continuing compliance requirements as of June 30, 2008 along with the value of total outstanding and new loans made during the current year in the schedule. The following is a summary of the loan programs maintained by the City and their balances at June 30, 2008:

Program Title	CFDA Number	Amount Outstanding	Prior year loans with continuing compliance requirements	New Loans
Community Development Block Grants/ Entitlement Grants	14.218	$ 7,395,280	$ 6,966,710	$ 428,570
HOME Investment Partnerships Program	14.239	41,434,193	36,305,529	5,128,664
		$48,829,473	$43,272,239	$5,557,234

(7) AIRPORT EXPENDITURES

The Federal Aviation Administration reimburses the Airport for approximately 80% of allowable Airport Improvement Program (AIP) grant expenditures. The remaining unreimbursed portion of grant expenditures, if eligible, are reimbursed from PFC revenue. Total allowable AIP expenditures are presented in the accompanying SEFA.

The accompanying schedule of revenues and expenditures of passenger facility charges includes approximately 20% of expenditures reimbursed by PFC revenue for AIP approved projects and 100% for non-AIP approved projects.

(8) SAN JOSE AREA WATER RECLAMATION & REUSE PROGRAM

The San José Area Water Reclamation & Reuse Program assists the City and tributary agencies of the San José-Santa Clara Water Pollution Control Plant in protecting endangered species habitats, achieving federally mandated water quality standards and reducing reliance on area surface, ground water, and imported water supplies. The U.S. Department of Interior – Bureau of Reclamation awarded the City $32.5 million in federal fiscal year 1995 and approved an increase of $2.5 million in federal fiscal year 2000. Funding for subsequent years, up to $35 million, is contingent upon subsequent Congressional appropriations acts. As a result of the timing of the subsequent funding approvals, the City requests reimbursements for costs incurred in prior fiscal years.

As of September 30, 2008, Congress appropriated $28,070,300 and the City has claimed cumulative reimbursements of $27,100,300 of which $484,252 was claimed in fiscal year 2008 for expenditures incurred prior to fiscal years. At June 30, 2008, the City has recorded a reimbursement request receivable in the amount of $970,000 that is awaiting final approval from the State Water Resources Control Board (SWRCB), the administering agent for the U.S. Department of the Interior.

(9) HOMELAND SECURITY CLUSTER

The City is a recipient of 2005, 2006, and 2007 Urban Areas Security Initiative (UASI) grant awards (CFDA 97.008). Per the 2008 *A-133 Compliance Supplement*, UASI grant awards for the specified grant years listed above are part of the Homeland Security Cluster under CFDA 97.067. In addition, the City incurred federal expenditures under the State Homeland Security Grant Program (HSGP) (CFDA 97.067) and Metropolitan Medical Response System (MMRS) (CFDA 97.067) which are also part of the Homeland Security Cluster program.

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CITY OF SAN JOSE, CALIFORNIA

Federal Awards Schedule of Findings and Questioned Costs

Year Ended June 30, 2008

Section I Summary of Auditor's Results

Financial Statements

Type of auditor's report issued on the basic financial statements of the City:	Unqualified
Internal control over financial reporting:	
♦ Material weakness(es) identified?	No
♦ Significant deficiencies identified that are not considered to be material weaknesses?	Yes
Noncompliance material to the financial statements noted?	No

Federal Awards

Internal control over major programs:	
♦ Material weakness(es) identified?	No
♦ Significant deficiencies identified that are not considered to be material weaknesses?	None reported
Type of auditor's report issued on compliance for major programs:	Unqualified
Any audit findings disclosed that are required to be reported in accordance with section 510(a) of OMB Circular A-133?	No

Identification of major programs:

Federal Catalog Number	Name of Federal Program or Cluster
14.239	Home Investment Partnerships Program
16.710	Public Safety Partnership and Community Policing Grants
20.106	Airport Improvement Program
20.205	Highway Planning and Construction
97.008/97.067	Homeland Security Cluster

Dollar threshold used to distinguish between type A and type B programs:	$1,867,213
Auditee qualified as a low-risk auditee?	No

Section II Financial Statement Findings

Item #2008-A - Workers' Compensation Claims Control

The City administers a self-insured workers' compensation program and is responsible for paying its employees' workers' compensation claims and related administrative expenses. Once an employee files a workers' compensation claim, the City estimates the total amount of the claim and records this amount in its workers' compensation claims database system. The City relies on its workers' compensation claims database reports to estimate its obligations and funding requirements and as such it is imperative that it maintains current and accurate documentation supporting the amounts included in its database.

The City designated the Human Resources Department (HRD) as the unit responsible for administering the City's workers' compensation program. Prior to FY2007-08, the City's claims adjusters were responsible for more cases compared to the industry norm. During FY2007/08, HRD hired 5 additional claims adjusters. However, the City was unable to fully integrate the new adjusters into its operating environment at the beginning of the year which resulted in the following exceptions on our tests of controls over 45 active case files out of population of 4,277 active case files:

- *Internal Control Exceptions:*
  - 6 claim files that are closed by the adjusters were not properly reflected in the Claims Management System and were shown as open cases with reserve balances.
  - 5 claim files had reserve amounts modified in the Claims Management System without updating the supporting documentation.

- *Compliance with State Laws and/or Regulations Exceptions:*
  - 3 claim files did not include the Doctor's First Response Reports (Form 5021) on file.

The City should continue to evaluate its process of closing of cases to ensure that all close cases are properly removed from the Claims Management Systems to avoid overstatement of the reserve balance and the worker's compensation claims liability. The City should also evaluate its training program to ensure that it has the appropriate level of expertise to ensure that the controls over the database system claims information are adequate to meet financial reporting and State compliance requirements.

Management Response:

In the fiscal year 2007-08 budget, the Human Resources Department (HRD) was authorized to hire 5 additional adjusters. The recruitment process was not complete until the second half of the fiscal year. Given the time constraint, the newly hired staff was unable to fully catch up with the backlog of work. However, the HRD anticipates that staff will be able to function at its optimum level capacity during fiscal year 2008-09. HRD is in the process of updating the closed case process and expects that the additional trained staff will alleviate the backlog and ensure that all closed cases are properly removed from the Claims Management System and that controls over the claims information in the database system are adequate to meet financial reporting and State compliance requirements.

Section III Federal Award Findings and Questioned Costs

None reported.

CITY OF SAN JOSE, CALIFORNIA

Passenger Facility Charges Schedule of Findings and Questioned Costs

Year Ended June 30, 2008

Section I Summary of Auditor's Results

Financial Statements

Type of auditor's report issued on the basic financial statements of the City:	Unqualified
Internal control over financial reporting:	
♦ Material weakness(es) identified?	No
♦ Significant deficiencies identified that are not considered to be material weaknesses?	Yes
Noncompliance material to the financial statements noted?	No

Passenger Facility Charges

Internal control over Passenger Facility Charges:	
♦ Material weakness(es) identified?	No
♦ Significant deficiencies identified that are not considered to be material weaknesses?	None reported
Type of auditor's report issued on compliance for the Passenger Facility Charges program:	Unqualified
Any audit findings disclosed that are required to be reported in accordance with section 510(a) of OMB Circular A-133 in relation to the Passenger Facility Charge program?	No

Section II Financial Statement Findings

See Financial Statement Finding Item #2008-A in Federal Awards Schedule of Findings and Questioned Costs.

Section III Passenger Facility Charges Findings and Questioned Costs

None reported.

Reference Number:	**2007-A – Housing Loan Reserves Calculations**
Audit Finding:	The Housing Department's loan portfolio analysis included a computation error resulting in a potential understatement of the loan loss reserves.
Status of Corrective Action:	Partially corrected. The City performed a thorough review of its loan portfolio and re-evaluated the methodology for the loan loss reserves calculations. Loan loss reserve calculations are heavily dependent on the type of loans and the loans' maturity dates. During FY 2008, we noted that the maturity dates of some loans are not accurate, which led to inaccurately calculated loan loss reserves. See matter reported to management of the City in a separate letter dated October 8, 2008.
Reference Number:	**2007-B – Internal Controls Over Financial Reporting**
Audit Finding:	The current lack of resources, particularly those devoted to financial reporting, has resulted in financial statement drafts containing numerous errors and requiring more review time by the external auditors.
Status of Corrective Action:	Corrected.
Reference Number:	**2007-C – Workers' Compensation Claims Control**
Audit Finding:	The current lack of resources, particularly adjuster positions, has resulted in database system claims information not properly supported and reviewed to meet financial reporting and State compliance requirements.
Status of Corrective Action:	See current year finding 2008-A.
Reference Number:	**2007-1**
Federal Catalog Number/ Program Name:	U.S. Department of Housing and Urban Development 14.241 / Housing Opportunities for Persons with AIDS U.S. Department of Transportation Passthrough the California Department of Transportation 20.205 / Highway Planning Construction U.S. Department of Homeland Security Passthrough the California Office of Emergency Services 97.008 / Urban Areas Securities Initiatives
Audit Finding:	During our audit we noted that the City included misstatements in its final draft schedule of expenditures of federal awards (SEFA) for the above programs, resulting in the SEFA not being accurate.
Status of Corrective Action:	Corrected.

CITY OF SAN JOSE, CALIFORNIA

Summary Schedule of Prior Audit Findings

Year Ended June 30, 2008

Reference Number:	**2007-2**
Federal Catalog Number/ Program Name:	U.S. Department of Transportation Passthrough the California Department of Transportation 20.205 / Highway Planning and Construction U.S. Department of Homeland Security Passthrough the California Office of Emergency Services 97.008 / Urban Areas Security Initiative (UASI)
Audit Finding:	The City's Department of Transportation and the Office of Emergency Services did not perform monitoring procedures over its subrecipients as required by Federal grant requirements.
Status of Corrective Action:	Corrected.
Reference Number:	**2007-3**
Federal Catalog Number/ Program Name:	U.S. Department of Transportation Passthrough the California Department of Transportation 20.205 / Highway Planning and Construction
Audit Finding:	During our audit, we noted that the City did not verify whether the potential contractor was not suspended or debarred or otherwise excluded when a procurement contract was made.
Status of Corrective Action:	Corrected.